

APPENDIX A
THE STATE OF CALIFORNIA



NOTE: Since the date of the Preliminary Official Statement, certain information in Appendix A has been updated, shown in *italics* on the following pages: A-5 through A-9, A-12, A-56, A-87, A-88, A-129, A-144, A-146, A-147 and A-153.

March 12, 2014

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INTRODUCTION TO THE STATE OF CALIFORNIA AND APPENDIX A

APPENDIX A is the part of the Official Statement that provides investors with information concerning the State of California. This Introduction is intended to give readers a very brief overview of the main topics covered in APPENDIX A. Investors are advised to read the entire Official Statement, including APPENDIX A, to obtain information essential to making an informed investment decision. See “Certain Defined Terms” at the end of this section for certain defined terms used in this APPENDIX A.

State Financial Condition

During the recent recession, which officially ended in 2009, the state experienced the most significant economic downturn since the Great Depression of the 1930s. As a result, state tax revenues declined precipitously, resulting in large budget gaps and occasional cash shortfalls in the period from 2008 through 2011.

The state enacted and maintained significant spending reductions in the past three budgets and voters in 2012 approved Proposition 30 providing increased revenues through the next several fiscal years. As of the 2014-15 Governor’s Budget, the state’s budget is projected to remain balanced within the projection period ending in fiscal year 2017-18. See “PROPOSED FISCAL YEAR 2014-15 BUDGET – Multi-Year Budget Projections.”

Despite the recent significant budgetary improvements, there remain a number of major risks and pressures that threaten the state’s financial condition, including the need to repay billions of dollars of obligations which were deferred to balance budgets during the economic downturn. See “DEFERRED OBLIGATIONS” and “CURRENT STATE BUDGET – Budget Risks.” In addition, the state’s revenues (particularly the personal income tax) can be volatile and correlate to overall economic conditions. There can be no assurances that the state will not face fiscal stress and cash pressures again, or that other changes in the state or national economies will not materially adversely affect the financial condition of the state.

State Revenues, Expenditures and Cash Management

The state receives revenues from taxes, fees and other sources, the most significant of which are the personal income tax, sales and use tax, and corporation tax (which collectively constitute over 90 percent of total General Fund revenues and transfers). The state expends money on a variety of programs and services. Significant elements of state expenditures include education (both kindergarten through twelfth grade (“K-12”) and higher education), health and human services, and correctional programs. For a discussion of the sources and uses of state funds, see “STATE FINANCES.”

The 2013 Budget Act and related legislation (the “2013-14 Budget”) provided for a multi-year General Fund plan that was balanced and projected a \$1.1 billion reserve by the end of fiscal year 2013-14. The 2014-15 Governor’s Budget now projects that the state will end fiscal year 2013-14 with a reserve of \$3.257 billion. See “CURRENT STATE BUDGET”.

The 2014-15 Governor's Budget proposes a multi-year General Fund strategy that is structurally balanced, significantly pays down the unprecedented level of budgetary borrowings, debts and deferrals which were accumulated in order to balance budgets largely over the past decade ("wall of debt"), and projects the "wall of debt" would be fully eliminated by the end of fiscal year 2017-18. See "DEFERRED OBLIGATIONS." Additionally, for the first time since 2007-08, the budget includes a transfer into the Budget Stabilization Account ("BSA" or "rainy day fund"). For more information on the Governor's proposed budget plan, see "PROPOSED FISCAL YEAR 2014-15 STATE BUDGET."

The state manages its cash flow requirements during the fiscal year primarily with a combination of external borrowing and internal borrowing by the General Fund from over 700 special funds. Since June 2008, the General Fund has typically ended each fiscal year with a net borrowing from these special funds. As of June 30, 2013, the General Fund owed \$2.435 billion to these special funds and other state funds from internal borrowing for cash management purposes (compared to almost \$9.593 billion owed at June 30, 2012 and \$8.165 billion at June 30, 2011). See "STATE FINANCES – Inter-Fund Borrowings."

General Fund

The moneys of the state are segregated into the General Fund and over 1,000 other funds, including special, bond and other funds. The General Fund consists of revenues received by the State Treasury and not required by law to be credited to any other fund, as well as earnings from the investment of state moneys not allocable to another fund. The General Fund is the principal operating fund for the majority of governmental activities and is the depository of most of the major tax revenue sources of the state. For additional financial data relating to the General Fund, see the State Controller's unaudited reports of General Fund cash receipts and disbursements attached to this APPENDIX A as EXHIBIT 1 and EXHIBIT 2 and the audited financial statements in APPENDIX F to this Official Statement. See "STATE FINANCES" and "FINANCIAL STATEMENTS."

The state Constitution specifies that an annual budget shall be proposed by the Governor by January 10 of each year for the next fiscal year (the "Governor's Budget"). Under state law, the annual proposed Governor's Budget cannot provide for projected expenditures in excess of projected resources for the ensuing fiscal year. State law also requires the Governor to update the Governor's Budget projections and budgetary proposals by May 14 of each year (the "May Revision"). The May Revision is normally the basis for final negotiations between the Governor and Legislature to reach agreement on appropriations and other legislation to fund state government for the ensuing fiscal year (the "Budget Act"). The state Constitution calls for adoption of a balanced budget by a majority vote of each House of the Legislature (the vote requirement had been two-thirds prior to 2011) by June 15 of each year. The Governor has 12 calendar days to either sign or veto the enrolled budget.

Over the years, a number of laws and constitutional amendments have been enacted, often through voter initiatives, which have made it more difficult for the state to raise taxes, restricted the use of the General Fund or special fund revenues, or otherwise limited the Legislature and the Governor's discretion in enacting budgets. See "THE BUDGET PROCESS – Constraints on the Budget Process."

State Indebtedness and Other Obligations

As of February 1, 2014, the state had outstanding obligations payable principally from the state's General Fund or from lease payments paid from the operating budget of the respective lessees, which operating budgets are primarily, but not exclusively, derived from the General Fund, consisting of \$75.2 billion principal amount of general obligation bonds and \$10.2 billion of lease-revenue bonds. As of February 1, 2014, there was approximately \$27.6 billion of authorized and unissued long-term voter-approved general obligation bonds payable principally from the General Fund and approximately \$5.87 billion of authorized and unissued lease revenue bonds. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Future Issuance Plans; General Fund Debt Ratio."

Certain state agencies and authorities issue revenue obligations for which the General Fund has no liability. Revenue bonds represent obligations payable from state revenue-producing enterprises and projects, which are not payable from the General Fund, and conduit obligations payable only from revenues paid by local governments or private users of facilities financed by the revenue bonds.

California has always paid when due the principal of and interest on all its debts, including general obligation bonds, general obligation commercial paper notes, lease-revenue obligations and short term obligations, including revenue anticipation notes ("RANs") and revenue anticipation warrants ("RAWs"). Detailed information regarding the state's long-term debt appears in the sections "STATE INDEBTEDNESS AND OTHER OBLIGATIONS" and "STATE DEBT TABLES."

Deferred Obligations

In addition to the bonds and other obligations described in the preceding paragraphs, as part of budget solutions in prior fiscal years the state engaged in budgetary actions which created pressures or repayment obligations upon the General Fund in future years. Over a number of years, the state adopted budget solutions for a fiscal year by deferring certain required payments (including Proposition 98 payments to schools, Medi-Cal reimbursements, state payrolls and payments to the state pension fund) from that fiscal year into the next year; ultimately these deferrals are being repeated year after year until paid. In addition, the General Fund is the ultimate source of repayment of deficit bonds ("ERBs"), and is obligated for certain legislatively-approved interfund borrowings (loans from special funds), reimbursement of borrowings from state and local governments, reimbursements to local governments and school districts for the costs of state mandates placed on those entities under state laws, settle-up payments for Proposition 98, payments to employees for compensated absences, costs for self insurance, and future payment of interest owed on borrowings from the federal government for unemployment insurance payments. (In some cases, the Legislature has the ability to modify, further extend the timing of or even cancel the repayment of some of these obligations.) See "DEFERRED OBLIGATIONS," including Table 7.

The 2014-15 Governor's Budget proposes to significantly pay down inter-year deferrals. At the 2013 Budget Act, the total amount of deferrals and legislatively-approved budgetary borrowing from special funds (as contrasted to short-term borrowing from special funds for cash

management purposes) was projected to be \$24.9 billion by the end of fiscal year 2013-14. The 2014-15 Governor's Budget includes further reductions in such deferred obligations of over \$11 billion by the end of fiscal year 2014-15, leaving a balance of \$13.9 billion. The Administration projects that all outstanding budgetary borrowing and deferrals would be entirely repaid by the end of fiscal year 2017-18.

As of the 2014-15 Governor's Budget, in addition to the Proposition 98 budgetary deferrals and settle-up payments referred to above (and set forth in Table 7), the General Fund is obligated to repay school and community college districts for past underfunding which is permitted under Proposition 98 ("maintenance factor"). The Department of Finance estimates that the total outstanding balance at the end of fiscal year 2013-14 for the Proposition 98 maintenance factor would be \$7.9 billion. The outstanding balance at the end of fiscal year 2014-15 is projected to be \$4.5 billion. The Proposition 98 maintenance factor is repaid pursuant to the constitutional repayment formula in years when growth in per capita General Fund revenue outpaces growth in per capita personal income. See "STATE FINANCES – Proposition 98 and K-14 Funding."

State Pension Funds and Retiree Health Care Costs

The two main state pension funds sustained substantial investment losses in recent years and, despite positive investment returns in 2013, still face large unfunded future liabilities. CalPERS reported an unfunded accrued liability allocable to state employees (excluding judges and elected officials) as of June 30, 2012, of \$28.2 billion on an actuarial value of assets ("AVA") basis (an increase of \$1.0 billion from the June 30, 2011 Valuation) and \$45.5 billion on a market value of assets ("MVA") basis (an increase of \$7.0 billion from the June 30, 2011 Valuation). The California State Teachers' Retirement System ("CalSTRS") reported the unfunded accrued liability of its Defined Benefit Plan as of June 30, 2012 at \$71.0 billion on an AVA basis (an increase of \$6.5 billion from the June 30, 2011 valuation), and \$80.4 billion on an MVA basis (an increase of \$12 billion from the June 30, 2011 valuation).

General Fund contributions to CalPERS and CalSTRS are estimated in the 2014-15 Governor's Budget to be approximately \$2.3 billion and \$1.4 billion, respectively. The combined contributions, which include contributions for California State University ("CSU"), represent about 3.5 percent of all General Fund expenditures in fiscal year 2014-15. See "PROPOSED FISCAL YEAR 2014-15 BUDGET." There can be no assurances that the state's annual required contributions to CalPERS and CalSTRS will not significantly increase in the future. The actual amount of any increases will depend on a variety of factors, including but not limited to investment returns, actuarial assumptions, experience, retirement benefit adjustments, and, in the case of CalSTRS, statutory changes in contributions. Recent action by the CalPERS Board to revise amortization and smoothing policies is expected to result in more rapid increases in state retirement contributions commencing in fiscal year 2015-16. The Board in February 2014 also adopted staff recommendations to change mortality and other assumptions, which will result in increased contribution rates starting in fiscal year 2014-15. See "PENSION TRUSTS—Prospective Funding Status; Future Contributions."

The state also provides postemployment health care and dental benefits to state employees and their spouses and dependents (when applicable) and utilizes a "pay-as-you-go"

funding policy. These are sometimes referred to as Other Post Employments Benefits or “OPEB.” As reported in the state’s OPEB Actuarial Valuation Report, the state has an Unfunded Actuarial Accrued Liability relating to state retirees’ other postemployment benefits which was estimated at \$64.57 billion as of June 30, 2013 (as compared to \$63.84 billion estimated as of June 30, 2012). See “STATE FINANCES – Retiree Health Care Costs.”

Financial Statements

APPENDIX F to this Official Statement, which is incorporated into this APPENDIX A, contains the Audited Basic Financial Statements of the state for the year ended June 30, 2012, together with certain information required by governmental accounting and financial reporting standards to be included in the Financial Statements, including a “Management’s Discussion and Analysis” that describes and analyzes the financial position of the state and provides an overview of the state’s activities for the fiscal year ended June 30, 2012. See “FINANCIAL STATEMENTS.”

In addition, EXHIBIT 1 and EXHIBIT 2 to APPENDIX A contains the State Controller’s unaudited reports of General Fund cash receipts and disbursements for the period July 1, 2012 through June 30, 2013 and for the period *July 1, 2013 through February 28, 2014, respectively.*

Population and Economy of the State

The State of California is by far the most populous state in the nation, nearly 50 percent larger than the second-ranked state according to the 2010 U.S. Census. The 2013 estimate of California’s population is 38.2 million residents, which is 12 percent of the total United States population.

California’s economy, the largest among the 50 states and one of the largest and most diverse in the world, has major components in high technology, trade, entertainment, agriculture, manufacturing, government, tourism, construction and services. The relative proportion of the various components of the California economy closely resembles the make-up of the national economy.

The California economy is experiencing a gradual and broadening recovery. Continued growth in the high-technology sector, international trade, and tourism are being supplemented by better residential construction and real estate conditions.

Demographic and economic statistical information and a discussion of economic assumptions are included in this APPENDIX A under “PROPOSED FISCAL YEAR 2014-15 BUDGET – Economic Assumptions Underlying the Forecast for the 2014-15 Governor’s Budget” and “ECONOMY AND POPULATION.”

Certain Defined Terms

The following terms and abbreviations are used in this APPENDIX A:

“Administration” means the Governor’s Office and those individuals, departments, and offices reporting to it (including the Department of Finance).

“2012 Budget Act” means the Budget Act for fiscal year 2012-13, adopted on June 27, 2012.

“2012-13 Budget” means the 2012 Budget Act plus related legislation to implement the budget.

“2013-14 Governor’s Budget” means the Governor’s Proposed Budget for fiscal year 2013-14 released on January 10, 2013.

“2013-14 May Revision” means the May Revision of the 2013-14 Governor’s Budget released on May 14, 2013.

“2013 Budget Act” means the Budget Act for fiscal year 2013-14, adopted on June 27, 2013.

“2013-14 Budget” means the 2013 Budget Act plus related legislation to implement the budget.

“2014-15 Governor’s Budget” means the Governor’s Budget for fiscal year 2014-15 released on January 9, 2014.

“BSA” means the Budget Stabilization Account created under Proposition 58. See “STATE FINANCES – Budget Reserves.”

“ERBs” means Economic Recovery Bonds of the state issued pursuant to Proposition 57. See “STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Economic Recovery Bonds.”

“EXHIBIT 1” means the State Controller’s Unaudited Statement of General Fund Cash Receipts and Disbursements for the period from July 1, 2012 through June 30, 2013 as attached to this APPENDIX A as EXHIBIT 1.

“EXHIBIT 2” means the State Controller’s Unaudited Statement of General Fund Cash Receipts and Disbursements for the period from July 1, 2013 through *February 28, 2014* as attached to this APPENDIX A as EXHIBIT 2.

“LAO” means the Legislative Analyst’s Office, an entity of the State Legislature.

“Proposition 30” means The Schools and Local Public Safety Protection Act of 2012, an initiative measure which was approved by the voters in the November 2012 statewide general election ballot. See “STATE FINANCES – Sources of Tax Revenue.”

“Proposition 39” means the California Clean Energy Jobs Act, an initiative measure which was approved by the voters in the November 2012 statewide general election ballot. See “STATE FINANCES – Sources of Tax Revenue.”

“SB 105” means Senate Bill 105 (Chapter 310, Statutes of 2013), providing additional appropriations in fiscal year 2013-14 to address a court-ordered reduction of the prisoner population in state prisons.

“SFEU” means the Special Fund for Economic Uncertainties, created pursuant to Government Code Section 16418.

Reference to the “state” as a noun or adjective means the State of California, following the practice of the Department of Finance.

RECENT DEVELOPMENTS

The following significant developments have occurred since the previous state Appendix A released in November 2013.

2014-15 Governor’s Budget. On January 9, 2014, the Governor’s proposed budget was released. The proposal continues to pay down the “wall of debt”, while continuing to invest in public schools and expand health care coverage for millions. The proposal also includes a deposit in the state’s rainy day fund (BSA). See “PROPOSED FISCAL YEAR 2014-15 BUDGET”.

Subsequent to the release of the 2014-15 Governor’s Budget, a \$274 million error involving an overstatement of personal income tax accruals for fiscal year 2011-12 and prior years was discovered by the Administration. This resulted in a \$274 million overstatement of the 2012-13 beginning fund balance and the Special Fund for Economic Uncertainties.

Recent Tax Receipts. The Department of Finance reported that, based on agency cash receipts, tax receipts for January, 2014 were \$90 million above the 2014-15 Governor’s Budget forecast of \$12.229 billion. *Revenues through January were \$131 million above the expected \$55.472 billion.*

The Department of Finance reported that, based on agency cash receipts, tax receipts for February, 2014 were \$825 million above the 2014-15 Governor’s Budget forecast of \$3.223 billion. Year-to-date revenues, which include a \$9 million positive adjustment to January revenues, are \$965 million above the expected \$58.695 billion.

Recent CalPERS Action. On February 20, 2014, the CalPERS Board of Administration adopted new mortality and retirement assumptions as part of a regular review of demographic experience. The impact of the assumption changes will be phased-in over three years, with a twenty year amortization, beginning in fiscal year 2014-15. The state estimates these changes will increase the state’s retirement contribution by an additional \$430.1 million (\$254.2 million from the General Fund) in fiscal year 2014-15, with additional expected increases in the following two years. See “PENSION TRUSTS – CalPERS - Actuarial Assumptions.”

Court Ordered Release of State Inmates. In connection with long-standing litigation concerning prisoner health care, which had resulted in court orders for the state to reduce its prison population by early in 2014, on February 10, 2014, the federal three-judge panel granted the state’s request to extend the deadline for meeting the population cap of 137.5 percent of the prisons’ design capacity until February 28, 2016, subject to a number of conditions. See “STATE FINANCES – California Department of Corrections and Rehabilitation” and “LITIGATION – Prison Healthcare Reform and Reduction of Prison Population.”

Drought Declaration by the Governor. The state is experiencing record dry conditions. Snowpack in California's mountains is severely below average through February 2014, and California's largest water reservoirs have very low water levels for this time of year. On January 17, 2014, Governor Brown proclaimed a State of Emergency and directed state officials to take all necessary actions to prepare for these drought conditions. The State of California Department of Water Resources has reduced water allocations from the State Water Project and the U.S. Bureau of Reclamation has announced reduced water allocations from the federal Central Valley Project for 2014. The Legislature *passed and the Governor signed* emergency legislation to provide over \$680 million (of which \$541 million is from existing voter approved bonds) for drought relief efforts, such as assisting citizens disproportionately impacted by the drought and supporting local and regional water supply and conservation projects. As the drought evolves, the Administration will be monitoring the situation.

PROPOSED FISCAL YEAR 2014-15 BUDGET

General

The 2014-15 Governor's Budget, released on January 9, 2014, proposes a multi-year plan that is balanced, and pays down budgetary debt from past years.

General Fund revenues and transfers for fiscal year 2014-15 are projected at \$104.5 billion, an increase of \$4.4 billion or 4.3 percent compared with revised estimates for fiscal year 2013-14. General Fund expenditures for fiscal year 2014-15 are projected at \$106.8 billion, an increase of \$8.3 billion or 8.5 percent compared with revised estimates for fiscal year 2013-14. The projected excess of expenditures over revenues and transfers is due in part to the budgetary accounting treatment of the BSA transfer, described in the next paragraph, and to the allocation of revenues to pay down "wall of debt" liabilities. See Table 3.

For the first time since the 2007-08 fiscal year, the Governor will allow full funding of the BSA during fiscal year 2014-15. Pursuant to Proposition 58 of 2004, the state will set aside 3% of estimated General Fund revenues, estimated at about \$3.2 billion, in the BSA. Under Proposition 58, half this amount will remain in the BSA, and half will be transferred to a redemption account to retire Economic Recovery Bonds (one of the components of the "wall of debt"). Under the state's budgeting procedures (and included in the figures in the previous paragraph), the \$1.6 billion transferred to the BSA for "rainy day" purposes will be reflected as a reduction of revenues and transfers, while the \$1.6 billion used to retire Economic Recovery Bonds will be reflected as an expenditure of General Fund resources. The Legislature cannot reduce or suspend the transfer to the BSA, but can increase the transfer. The Governor can modify the transfer up to June 1, 2014. See "STATE FINANCES – Budget Reserves – Budget Stabilization Account."

The 2014-15 Governor's Budget has the following other major components:

- Proposition 98 – proposes funding of \$61.6 billion for fiscal year 2014-15, of which \$45.1 billion is from the General Fund. When combined with General Fund increases of \$3.7 billion in 2012-13 and 2013-14, the Budget proposes a \$9.7 billion increase in the General Fund investment in K-14 education compared to the 2013-14 Budget. The Budget also proposes

to eliminate school budgetary deferrals in fiscal year 2014-15. See “STATE FINANCES – Proposition 98 and K-14 Funding”.

- Higher Education – proposes total state funding of \$12.8 billion for all major segments of Higher Education, including \$12.4 billion from the General Fund (both Non-Proposition 98 and Proposition 98), an increase of \$1.2 billion General Fund from revised estimates for fiscal year 2013-14. The remaining funds include special and bond funds.

- Health and Human Services – proposes \$48.1 billion, including \$28.8 billion General Fund and \$19.3 billion from special funds, for these programs. See “STATE FINANCES – Health and Human Services.”

- Implementation of the Affordable Care Act – proposes \$7.6 billion, including \$250.8 million from the General Fund, to implement federal health care reform, which started in January 2014, and will provide coverage to millions of Californians. See “STATE FINANCES – Health and Human Services – Health Programs – Health Care Reform.”

- Prison Funding – proposes total state funding of \$12.0 billion, including \$9.6 billion from the General Fund and \$2.4 billion from special funds, for the Department of Corrections and Rehabilitation. On February 10, 2014, the federal three-judge panel granted the state’s request to extend the deadline for meeting the population cap of 137.5 percent of design capacity until February 28, 2016. The proposed budget assumed this two year extension would be granted. See “STATE FINANCES – California Department of Corrections and Rehabilitation” and “LITIGATION – Prison Healthcare Reform and Reduction of Prison Population.”

- Redevelopment Agency Dissolution Savings – proposes Proposition 98 General Fund savings of \$1.1 billion in fiscal year 2013-14 and \$785 million in fiscal year 2014-15. This reflects the receipt of a like amount of property tax revenues in each fiscal year by K-12 schools and community colleges.

- Payment of Interest on Unemployment Insurance Fund Debt – proposes \$231.6 million from the General Fund to make the 2014 interest payment on the outstanding loan from the federal unemployment account. Interest will continue to accrue and be payable annually until the principal on the UI loan is repaid. The principal amount of the federal loan is projected to be \$8.8 billion at the end of calendar year 2014 *compared to \$9.7 billion at the end of 2013*. See “STATE FINANCES – Unemployment Insurance.”

- Cash Management – Cash flow needs will be managed through internal and external borrowing. The 2014-15 Governor’s Budget projects the need for \$3.5 billion in revenue anticipation notes, compared with \$5.5 billion in fiscal year 2013-14.

- Reserve Policy – the Governor’s Budget proposes a constitutional amendment to appear on the November 2014 ballot which would significantly amend the existing rainy day fund requirements established by Proposition 58. See “STATE FINANCES – Budget Reserves.”

The following table summarizes the General Fund in the 2014-15 Governor's Budget:

TABLE 1

General Fund Budget Summary

(Dollars in Millions)

	As of 2013 Budget Act Fiscal Year <u>2013-14</u>	As of 2014-15 Governor's Budget Fiscal Year <u>2013-14</u>	Fiscal Year <u>2014-15</u>
Prior Year Balance ^(a)	\$ 872	\$ 2,528	\$ 4,212
Revenues and Transfers	<u>97,098</u>	<u>100,147</u>	<u>104,503</u>
Total Resources Available	97,970	102,675	108,715
Non-Proposition 98 Expenditures	57,226	57,515	61,731
Proposition 98 Expenditures	<u>39,055</u>	<u>40,948</u>	<u>45,062</u>
Total Expenditures	96,281	98,463	106,793
Fund Balance ^(a)	1,689	4,212	1,922
Budget Reserves:			
Reserve for Liquidation of Encumbrances	618	955	955
Special Fund for Economic Uncertainties ^(a)	1,071	3,257	967
Budget Stabilization Account/ Rainy Day Fund			1,591

Source: State of California, Department of Finance.

^(a) In this table, for the 2014-15 Governor's Budget columns, beginning in 2013-14, this figure includes a \$274 million overstatement of personal income tax accruals for 2011-12 and prior years, an error identified by the Administration subsequent to the release of the Governor's Budget. This results in a \$274 million overstatement of the Fund Balance and the Special Fund for Economic Uncertainties.

Development of Revenue Estimates

Development of the forecast for the major General Fund revenues begins with a forecast of national economic activity prepared by an independent economic forecasting firm. The Department of Finance's Economic Research Unit, under the direction of the Chief Economist, adjusts the national forecast based on the Department of Finance's economic outlook. The national economic forecast is used to develop a forecast of similar indicators for California activity.

After finalizing the forecasts of major national and California economic indicators, revenue estimates are generated using revenue forecasting models developed and maintained by the Department of Finance. With each forecast, adjustments are made for any legislative, judicial, or administrative changes, as well as for recent cash flow results. The forecast is updated twice a year and released with the Governor's Budget by January 10 and the May Revision by May 14.

National Economy. The national economy continued to recover between April 2013, when the economic forecast for the 2013-14 May Revision was constructed, and November 2013, when the economic forecast for the 2014-15 Governor's Budget was developed. Various economic indicators suggest that the national economy experienced an uneven expansion in 2013, with a strong third quarter, and growth likely muted in the fourth quarter by the federal government shutdown. The recovery is expected to pick up in 2014 and 2015.

Following an annual growth rate of 1.1 percent in the first quarter of 2013, output of the national economy (Real Gross Domestic Product) grew by 2.5 percent in the second quarter and 4.1 percent in the third quarter of 2013 – the tenth consecutive quarter of growth. A decline in federal defense spending slowed economic growth in the first half of 2013. Retail sales grew 5.2 percent in 2012 and 4.1 percent in 2013. These numbers reflect the new national accounts methodology used by the U.S. Bureau of Economic Analysis.

The national unemployment rate declined gradually from the middle of 2011 through 2013, to 6.7 percent in December. Nonfarm payroll employment expanded at a modest pace from 2011 through the end of 2013. The expiration of long-term unemployment benefits at the end of December likely contributed to a drop in the labor force at the end of 2013, as discouraged job-seekers no longer had the incentive of unemployment benefits to remain in the labor force (defined as those employed or actively seeking work).

Home building has been gradually improving but is still relatively weak compared to pre-crisis levels and historical averages. New home construction increased modestly in 2011 and then accelerated sharply in 2012. While still at a subdued level with respect to pre-crisis levels, housing starts were up over 18 percent during 2013. Home prices in most metropolitan areas were improving in 2013.

U.S. exports of goods were up 2.6 percent during the first eleven months of 2013 compared to the same period in 2012, which contributed to a shrinking trade deficit.

California Economy. California's recovery spread to more sectors of the economy in 2013. Continued growth in the high-technology sector, international trade, and tourism are being supplemented by better residential construction and real estate conditions.

Personal income increased in thirteen of the fifteen quarters through the third quarter of 2013, with decreases only in the fourth quarter of 2011 and the first quarter of 2013. The decrease in early 2013 was partially due to the expiration of the federal payroll tax holiday. These numbers also reflect the revised methodology implemented by the U.S. Bureau of Economic Analysis for the national accounts. Although the reported levels of personal income have changed as a result of the revised methodology, these changes merely reflect more accurate statistics about the underlying state of the economy. As such, the changes will not have any impact on revenue. In the longer run, the more accurate economic data could lead to more accurate revenue forecasts.

California's nonfarm payroll jobs grew by 235,700 between December 2012 and December 2013, or by 19,600 jobs per month on average. In 2012, employment grew by 295,700, or by 24,600 jobs per month. During the first six months of 2013, payroll jobs grew by

82,800, or by 13,800 jobs per month. During the last six months of 2013, payroll jobs grew by 152,900, or by 25,500 jobs per month. The state unemployment rate reached a high of 12.4 percent in late 2010. The rate improved thereafter, falling to 8.3 percent in December 2013. In comparison, the national unemployment rate was 6.7 percent in December 2013.

After hitting a low of close to 200,000 units (seasonally-adjusted and annualized) in the middle of 2007, sales of existing single-family homes have rebounded to above 400,000 units annually. With limited inventories of homes for sale, existing home prices accelerated in the latter half of 2012. Home prices continued to climb in 2013 reaching levels not seen in more than five years. The median price of existing, single-family homes sold in December 2013 was \$438,040, an increase of \$100,980 from January 2013, and almost 20 percent higher than December 2012. However, this remains 26 percent below the pre-recession peak.

California issued 83,000 residential building permits in 2013, 42.6 percent more than were issued in 2012 but still only *39 percent* of the 213,000 permits issued in 2004.

The number of California homes going into foreclosure dropped to an eight-year low in the fourth quarter of 2013 at 18,120. That was down 10.8 percent from the prior quarter, and down 52.6 percent from the fourth-quarter of 2012. Foreclosures peaked in the first-quarter of 2009 at 135,431. The declining rate of foreclosure was likely due in part to the new state foreclosure laws (the “Homeowner Bill of Rights”) which took effect at the beginning of calendar year 2013.

California set a new record for merchandise exports in 2013. Export values totaled \$168.13 billion, surpassing the \$161.9 billion recorded in 2012. Exports of manufactured goods and non-manufactured goods (agricultural produce and raw materials) in 2013, were up 4.6 percent and 7.1 percent respectively, from 2012. For the month of December, California exports totaled \$14.6 billion, an increase of 9.3 percent from December 2012.

As in the rest of the nation, consumer spending in California rebounded in 2011 with growing vehicle sales playing a significant role. Taxable retail sales grew 9.1 percent in 2011 and 7.2 percent in 2012. New motor vehicle registrations in the first ten months of 2013 were up over 11 percent from the same time period in 2012.

The California economy is expected to continue making steady progress. Industry employment is forecast to expand 2.1 percent and 2.4 percent in 2013 and 2014, respectively, and 2.5 percent growth is projected for 2015. Personal income is projected to grow 2.2 percent in 2013, 5.7 percent in 2014 and 5.3 percent in 2015.

Despite moderate growth in the past year which appears to be continuing into the start of 2014, there are still risks to the economy. First, the persistence of unemployment has meant slow income growth for a broad section of the population, and slow wage growth. This impacts the ability of people to save and invest, and makes it difficult for consumption growth to support broader economic growth. Second, economic expansions do not last forever. In the post-war period, the average expansion length is almost five years and the longest expansion was ten years. As of December 2013, the current expansion has lasted four and a half years. There are

few immediate signs of a contraction, but it would be an historical anomaly for the U.S. not to see another recession before 2020.

Economic Assumptions Underlying Forecast for the 2014-15 Governor's Budget

The revenue and expenditure assumptions utilized in connection with the 2014-15 Governor's Budget are based upon certain projections of the performance of the California, national, and global economies in calendar years 2014 and 2015. These projections are set forth in the table below:

TABLE 2
Selected National and California Economic Data

	2013 (Estimated)	2014 (Projected)	2015 (Projected)
United States			
Real gross domestic product (2009 CW \$, percent change)	1.7	2.5	3.1
Personal income (percent change)	2.8	4.6	4.8
Nonfarm wage and salary employment (millions)	133.7	135.7	137.9
(percent change)	1.6	1.6	1.8
California			
Personal Income (\$ billions)	1,813.2	1,896.0	1,990.0
(percent change)	2.6	4.6	5.0
Nonfarm wage and salary employment (thousands)	14,707.0	15,043.0	15,384.6
(percent change)	2.1	2.3	2.3
Unemployment rate (percent)	8.9	7.9	7.3
Housing units authorized (thousands)	86.9	113.6	134.1
(percent change)	50.4	30.6	18.1
New auto registrations (thousands)	1,608.0	1,690.3	1,779.4
(percent change)	18.9	5.1	5.3
Total taxable sales (\$ billions)	587.5	625.1	666.1
(percent change)	5.8	6.4	6.6

CW: Chain Weighted

Note: Percentage changes calculated from unrounded data.

Source: State of California, Department of Finance, 2014-15 Governor's Budget.

Multi-Year Budget Projections

In connection with the preparation of the 2014-15 Governor's Budget, the Department of Finance prepared high level multi-year budget projections, as set forth below. The projections are based on a variety of assumptions, including assumptions concerning economic conditions, and state revenues and expenditures.

The year-to-year changes in Revenues and Transfers are driven, in general, by expected continued moderate economic growth. However, due largely to the strength of the stock market in 2013, capital gains are expected to be above normal levels for 2013 and 2014. As such, growth in tax receipts is expected to be higher than normal through 2014-15. Tax revenue is expected to grow by 8 percent from fiscal year 2013-14 to fiscal year 2014-15, and by 6 percent from fiscal year 2014-15 to fiscal year 2015-16. The growth rate for 2014-15 reflects the

reduction of fiscal year 2013-14 personal income tax revenue due to the acceleration of income into 2012 as a result of the federal tax landscape in late 2012 and early 2013.

For the following two fiscal years, underlying tax revenue is projected to grow at 4 percent a year. The other main factor explaining the year-to-year growth is the change in the amounts of loan repayment made each year consistent with the projection shown in Table 7 (Deferred Obligations). As indicated above, these projections show that, under the assumptions made, the state would be able to achieve a structural balance (positive “operating surplus”) for the next several years, while continuing to reduce Deferred Obligations (discussed in the next section). The reductions in this table are included as increases in expenditures. In the case of loan repayments, they are reductions in revenues and transfers. Actual conditions may differ materially from the assumptions, and there can be no assurances the projections will be achieved.

TABLE 3
General Fund Multi-Year Budget Projection

(Dollars in Millions)

	<u>2013-14</u>	<u>2014-15</u>	<u>Fiscal Year</u> <u>2015-16</u>	<u>2016-17</u>	<u>2017-18</u>
Prior Year Balance ^(a)	\$ 2,528	\$ 4,212	\$ 1,922	\$ 2,620	\$ 3,327
Revenues and Transfers ^(b)	100,147	106,094	111,436	117,421	123,168
Prop 58 Transfer to BSA		(1,591)	(1,000) ^(c)	(1,000) ^(c)	(1,000) ^(c)
Total Resources Available	\$102,675	\$108,715	\$112,358	\$119,041	\$125,495
Non-Proposition 98 Expenditures	57,515	60,140	63,234	67,500	71,187
Proposition 98 Expenditures	40,948	45,062	46,504	48,214	49,658
Prop 58 Transfer to BSA		1,591			
Total Expenditures	\$98,463	\$106,793	\$109,738	\$115,714	\$120,845
Fund Balance ^(a)	4,212	1,922	2,620	3,327	4,650
Reserve for Encumbrances	955	955	955	955	955
Special Fund for Economic Uncertainties ^(a)	3,257	967	1,665	2,372	3,695
Budget Stabilization Account (BSA)/Rainy Day Fund		1,591	2,591	3,591	4,591
Operating Surplus/Deficit with BSA Transfer	\$1,684	(\$2,290)^(d)	\$698	\$707	\$1,323

Source: State of California, Department of Finance

^(a) In this table, beginning in 2013-14, this figure includes a \$274 million overstatement of personal income tax accruals for 2011-12 and prior years, an error identified by the Administration subsequent to the release of the 2014-15 Governor’s Budget. This results in a \$274 million overstatement of the Fund Balance and the Special Fund for Economic Uncertainties.

^(b) The personal income tax portion of Proposition 30 expires after tax year 2018. Roughly one-half of the impact of Proposition 30 is expected to be lost in 2018-19, and beginning with 2019-20, there will be no remaining impact from the Proposition. The sales tax portion of Proposition 30 will expire after December 31, 2016.

^(c) Placeholder for transfers to the Budget Stabilization Account (rainy day fund), pending the outcome of the November 2014 election. See “STATE FINANCES – Budget Reserves”.

^(d) The 2014-15 operating deficit is largely the result of using the carry-in balance of \$4.2 billion to pay down “wall of debt” liabilities. See “DEFERRED OBLIGATIONS—Table 7”.

CURRENT STATE BUDGET

The information in this section generally contains information concerning fiscal year 2013-14 as of the adoption of the 2013 Budget Act in June, 2013, and the subsection “General” has not been revised to reflect actual results. See “ - Fiscal Year 2013-14 Revised Estimates in the 2014-15 Governor’s Budget” for a discussion of revised estimates for fiscal year 2013-14 as of the 2014-15 Governor’s Budget.

General

The 2013-14 Budget, including the 2013 Budget Act which was enacted on June 27, 2013, provided a multi-year General Fund plan that was balanced. For the then current fiscal year, at the time of budget enactment, it projected a \$1.1 billion reserve by year end, and continued to pay down budgetary debt from past years. For the first time in several years, corrective measures were not necessary to avoid a year-end deficit in the fiscal year just ended. On September 12, 2013, the Governor signed SB 105, appropriating an additional \$315 million during fiscal year 2013-14 to the Department of Corrections and Rehabilitation in response to a court-ordered requirement to further reduce the prison population. See “STATE FINANCES – California Department of Corrections and Rehabilitation.”

General Fund revenues and transfers for fiscal year 2013-14 were projected at \$97.1 billion, a decrease of \$1.1 billion or 1.1 percent compared with revised estimates for fiscal year 2012-13. General Fund expenditures for fiscal year 2013-14 were projected at \$96.3 billion, an increase of \$0.6 billion or 0.6 percent compared with revised estimates for fiscal year 2012-13. It should be noted that revenues, expenditures and reserve estimates are updated following the end of the fiscal year; therefore, these estimates are subject to change. For a discussion of updated information for fiscal year 2013-14 as of the 2014-15 Governor’s Budget, see “- Fiscal Year 2013-14 Revised General Fund Estimates in the 2014-15 Governor’s Budget.” Also, see Table 1 above for summary information concerning the estimated fund balance for fiscal year 2013-14 as revised in the 2014-15 Governor’s Budget.

The 2013-14 Budget built a \$1.1 billion reserve principally by using the following steps which reduced General Fund expenditures: suspending four newly identified state mandates (\$111 million), continuing the use of miscellaneous state highway account revenues to pay for transportation bond debt service (\$67 million); extending the hospital quality assurance fee (\$310 million); extending the gross premiums tax on Medi-Cal managed care plans (\$166 million); and applying sales tax on Medi-Cal managed care plans (\$305 million). Certain of these actions raised revenues in special funds which offset General Fund costs. Actions taken after enactment of the 2013 Budget Act may affect the final reserve amount. See “– Prison Funding” below.

As enacted, the 2013-14 Budget has the following significant components by major program area:

- Proposition 98 – The 2013-14 Budget provided Proposition 98 funding of \$55.3 billion for fiscal year 2013-14, of which \$39.1 billion was funded from the General Fund. Proposition 30 was premised on the need to reinvest in education. For the first time since the

recession began in 2008, with the passage of Proposition 30, the 2013 Budget Act reinvested in, rather than cuts, education funding. The 2013-14 Budget repaid approximately \$272 million in deferred payments to fund education programs and increased budget transparency.

In addition to revenues provided by Proposition 30, public schools and community colleges also benefited from the passage of Proposition 39. For fiscal year 2013-14, Proposition 39 raised approximately \$928 million in General Fund revenues, which increased the Proposition 98 guarantee level by an estimated \$558 million. Of this additional guarantee amount, \$456 million was being used to fund energy efficiency related activities in public schools and community colleges. See “STATE FINANCES – Proposition 98 and K-14 Funding.”

- Higher Education – The 2013-14 Budget included total funding of \$25.4 billion for all major segments of Higher Education, including \$13.1 billion from the General Fund and local property taxes for the California Community Colleges. The remaining funding was provided from state special and bond funds, student tuition and fee revenue, and other sources of income at the University of California, California State University, and the California Community Colleges. The 2013-14 Budget established the first-year investment in a multiyear stable funding plan for higher education.

Prior to fiscal year 2013-14, the state separately funded general obligation and lease revenue bond debt service for the University of California’s (“UC”) capital improvement projects. The 2013-14 Budget included a permanent shift of these appropriations into UC’s budget, and authorized UC to pledge its General Fund appropriation, within limits, in addition to its other revenue sources, towards the issuance of its revenue bonds to finance its infrastructure needs instead of using proceeds of state general obligation bonds or State Public Works Board (“SPWB”) lease revenue bonds. Any new capital expenditures were still subject to approval by the Administration and the Legislature, with limits on the amount that could be spent on capital expenditures from its General Fund appropriation.

- Health and Human Services – The 2013-14 Budget provided for total state funding for these programs of \$46 billion, including \$28.1 billion from the General Fund. The remaining funding was provided from special and bond funds.

As of the 2013 Budget Act, Medi-Cal, the state’s Medicaid health care program for low-income families, served one out of every five Californians, and received 16 percent of the General Fund budget. As the state implements its commitment to federal health care reform, these amounts will increase. The 2013 Budget Act included \$195.6 million from the General Fund to begin to pay for the federally required and optional expansion of coverage. See “– Health Care Reform” below.

- Prison Funding – The 2013 Budget Act provided for total state funding of \$11.2 billion, including \$8.9 billion from the General Fund, for the California Department of Corrections and Rehabilitation (“CDCR”). The CDCR total state operations costs were \$9.1 billion and the remaining \$2.1 billion support prison and jail infrastructure. SB 105, signed into law on September 12, 2013, appropriated an additional \$315 million from the General Fund to CDCR in fiscal year 2013-14 for purposes of complying with the court-ordered reduction in

prison population. See “STATE FINANCES – California Department of Corrections and Rehabilitation.”

- Redevelopment Agencies – As described in “STATE FINANCES – Local Governments,” legislation enacted in 2011 eliminated redevelopment agencies (“RDAs”) and replaced them with locally organized successor agencies tasked with retiring the former RDAs’ outstanding debts and other legal obligations. Elimination of RDAs will provide additional property tax funding for education, by capturing the RDA tax increment over and above the amounts needed to service existing debts of the RDAs. As of the 2013 Budget Act, the elimination of RDAs was projected to offset \$1.5 billion of Proposition 98 costs in fiscal year 2013-14, of which \$824 million was from property taxes which were distributed to local school districts, and \$707 million was from distribution of excess RDA cash.

- Other Revenues and Transfers – The Administration regularly monitors the needs of special funds to ensure that their purposes are not hindered by loans to the General Fund, and may defer (or accelerate) the repayments of such loans based on its review of the needs of the special funds. The 2013-14 Budget reflected a delay in repayment of approximately \$1 billion of loans scheduled for repayment in fiscal year 2013-14 (as projected in the 2012 Budget Act). Additionally, the 2013 Budget Act authorized a \$500 million loan to the General Fund from the Greenhouse Gas Reduction Fund (Cap and Trade). Both of these actions were reflected in the calculation of Deferred Obligations during fiscal year 2013-14. See “CURRENT STATE BUDGET – Cap and Trade Program.”

- Health Care Reform – With the coming implementation of the federal Affordable Care Act (“ACA”), health care costs will be an increasingly important element of the state budget. The 2013-14 Budget included \$195.6 million for costs relating to implementation of the ACA. General Fund net costs of expanded eligibility and enhanced benefits under health care reform are estimated to increase to approximately \$700 million in fiscal years 2014-15 and 2015-16 and they are included in the multi-year projection. Actual costs could be materially higher, as the program is implemented. For more detailed information about the state’s plans for implementation of the ACA. See “STATE FINANCES – Health and Human Services - Health Programs – Health Care Reform.”

- Unemployment Insurance Interest Repayment – For the last two fiscal years, the state had internally loaned money from special funds to pay the interest on money borrowed from the federal government to fund unemployment insurance payments. In fiscal year 2013-14, the interest payment of \$261.5 million was paid from the General Fund. (The General Fund is not liable for repayment of the principal of the federal loan.) See “STATE FINANCES – Unemployment Insurance.”

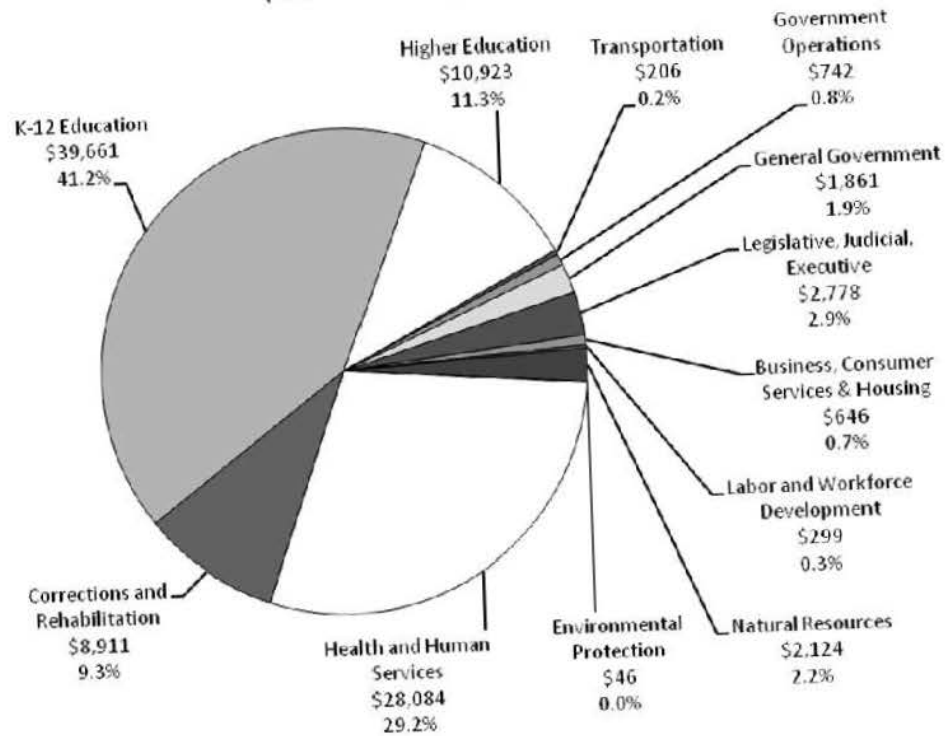
The following charts summarize the principal components of the 2013 Budget Act, as of its adoption.

In the chart below showing General Fund Expenditures, the state’s expenditures for contributions to the pension funds and for debt service on bonds are not shown separately, but are included within the applicable departmental/functional costs. The state’s contributions to CalPERS and CalSTRS in fiscal year 2013-14 were a combined \$3.7 billion, or 3.8 percent of

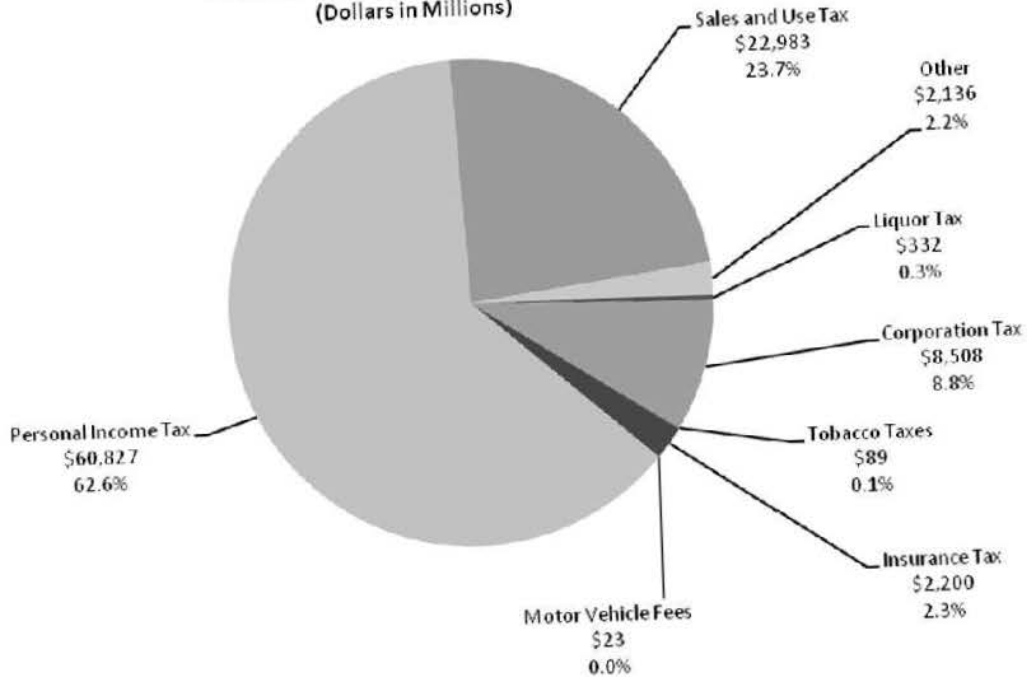
total expenditures from the General Fund. The net debt service costs on general obligation bonds and lease-revenue bonds paid by rental payments from the General Fund totaled \$5.693 billion, or 5.86 percent of total expenditures. These debt service costs were net of reimbursement from various special funds (e.g., vehicle weight fees offsetting costs of transportation bonds) and subsidy payments from the federal government for taxable Build America Bonds. See “STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Build America Bonds.”

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**2013-14
General Fund Expenditures
(Dollars in Millions)**



**2013-14
General Fund Revenues and Transfers
(Dollars in Millions)**



Fiscal Year 2013-14 Revised General Fund Estimates in the 2014-15 Governor's Budget

The 2014-15 Governor's Budget revised various estimates involving the General Fund beginning balance, revenues, and expenditures for fiscal year 2013-14. The 2014-15 Governor's Budget projects, based on the various assumptions and proposals it contains, a positive General Fund reserve balance of \$3,257 million at the end of fiscal year 2013-14, compared to the positive balance of \$1,071 million estimated at the end of the 2013-14 fiscal year when the 2013-14 budget was enacted. This increase of \$2.2 billion in the General Fund reserve for fiscal year 2013-14 is based on the following (please note that totals may not add because of rounding and that these figures are preliminary estimates subject to adjustment after receipt of additional information concerning revenues and expenditures for the year). In addition, please note these figures do not include the \$274 million overstatement of personal income tax accruals for fiscal year 2011-12 and prior years, an error identified by the Administration subsequent to the release of the Governor's Budget, as noted in footnote (a) of Table 1. See "PROPOSED FISCAL YEAR 2014-15 BUDGET."

1. Net gain of \$1.7 billion in beginning fund balance for fiscal year 2013-14 related to activities in the past year (fiscal year 2012-13) and prior years. This net gain in the starting balance for fiscal year 2013-14 is primarily due to the following components:

- \$1.7 billion increase in beginning balance due to higher than forecasted major revenues in the past year (fiscal year 2012-13);
- \$1.8 billion decrease in beginning balance due to higher than expected Proposition 98 spending related to the higher revenues mentioned above;
- \$0.6 billion net increase in beginning fund balance due to a net gain in overall revenues from prior years (fiscal year 2011-12 and prior fiscal years);
- \$0.4 billion decrease in beginning fund balance due to a Quality Education Investment Act payment for prior years to be appropriated in 2014-15;
- \$0.3 billion increase in beginning fund balance due to increase in 2012-13 encumbrances (resulting in lower spending). This is offset by a higher reserve for encumbrances, resulting in a net zero to the reserve.
- \$0.4 billion increase in the beginning fund balance due to Health and Human Services savings in 2011-12 and prior fiscal years; and
- \$0.9 billion increase in beginning fund balance due to various other past year and prior year adjustments.

2. General Fund revenues and transfers for fiscal year 2013-14 are projected at a revised \$100.1 billion, which is \$3 billion higher than the estimate of \$97.1 billion when the 2013-14 Budget was enacted. The increase is based on the following major factors:

- \$3.5 billion increase in personal income tax revenue; and

- \$0.5 billion decrease in corporation tax revenue.

3. General Fund expenditures for fiscal year 2013-14 are projected at \$98.5 billion, an increase of \$2.2 billion compared with the estimate of \$96.3 billion when the 2013-14 Budget was enacted. The net increase in expenditures is mainly attributable to the following:

- \$1.9 billion increase in Proposition 98 expenditures; and
- \$0.3 billion increase in Non-Proposition 98 expenditures, mainly because of increased spending in the Department of Corrections and Rehabilitation (prison population).

4. The reserve for encumbrance increased by \$0.3 billion since the enactment of the 2013-14 Budget.

Budget Risks

The 2013-14 Budget and the 2014-15 Governor's Budget are based on a variety of estimates and assumptions. If actual results differ from those assumptions, the state's financial condition could be adversely or positively affected. There can be no assurance that the financial condition of the state will not be materially and adversely affected by actual conditions or circumstances in fiscal years 2013-14, 2014-15 and beyond.

Budget risks with potential significant General Fund impact for fiscal years 2013-14 and 2014-15 include, but may not be limited to, the following:

- Threat of Recession — The two-year forecast assumes the continued modest economic expansion of the past couple of years. Yet, economic expansions do not last forever. In the post-World War II period, the average expansion has been about five years; the longest expansion was ten years. As of December 2013, the current expansion has lasted four-and-a-half years. While there are few signs of immediate contraction, the Administration understands that another recession is inevitable. In the past a recession has resulted in significant reductions in major state revenue sources.

- Federal Fiscal Challenges — Although the recent federal budget agreement provides greater stability to the federal government's fiscal situation, the federal government still faces both short- and long-term fiscal issues. In February 2014, Congress approved an increase in the federal debt limit, without any policy provisions attached. The increase is effective through March 15, 2015. As has been common in the past, the federal government could shift costs to the state to address its own fiscal challenges.

- Capital Gains Volatility — Capital gains are the state's most volatile revenue source. With a projected 10 percent of the General Fund revenues and transfers relying on capital gains in 2014-15, and 9.5 percent in 2013-14, the two-year forecast is heavily dependent on the continued performance of the stock market and, to a lesser extent, the real estate market.

- Redevelopment Dissolution — Between 2011-12 and 2014-15, cities, counties, special districts, and schools are estimated to receive over \$7 billion in revenues that previously would have been spent by redevelopment agencies. These dollars have been invested in core

local public services such as police and fire protection, and have been critical to the state balancing its budget. However, recent court decisions, if finalized and upheld, would put at risk approximately \$3 billion that accrued to the affected taxing entities from the Department of Finance's review of agency actions (of which approximately \$2 billion went to K-14 schools and resulted in a corresponding savings for the General Fund).

- Health Care Costs — Medi-Cal is the budget's second largest program. Additionally, the state provides health benefits to its own employees and retirees. As the state implements federal health care reform, budgetary spending will become even more dependent on the rate of health care inflation. If this inflation rises faster than expected, annual General Fund spending could quickly rise by hundreds of millions of dollars.

- Debts and Liabilities — The state's budget challenges have been exacerbated by the "wall of debt" — an unprecedented level of debts, deferrals, and budgetary obligations accumulated over the prior decade. Recent state budgets have reduced this debt from \$34.7 billion to \$24.9 billion (projected as of the end of 2013-14 at the enactment of the 2013-14 Budget). In addition, the state faces hundreds of billions of dollars in other long-term cost pressures, debts, and liabilities.

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Summary of State Revenues and Expenditures

The table below presents the actual revenues, expenditures and changes in fund balance for the General Fund for fiscal years 2010-11 and 2011-12, the estimated results for fiscal years 2012-13 and 2013-14 and the proposed amounts for fiscal year 2014-15. Note that at June 30, 2015, in addition to the Special Fund for Economic Uncertainties, part of the fund balance of the General Fund, there will be an estimated \$1.591 billion in the BSA. Consistent with historical practice, the beginning balance of any given fiscal year can be updated from time to time subsequent to initial projection to reflect changes attributable to preceding fiscal years. Changes affecting the beginning balance include both revenues and expenditures.

TABLE 4
Statement of Estimated Revenues, Expenditures,
and Changes in Fund Balance – General Fund
(Budgetary Basis)^(a)
Fiscal Years 2010-11 through 2014-15

	(Dollars in Millions)				
	2010-11	2011-12	Estimated^(b) 2012-13	Estimated^(b) 2013-14	Proposed^(b) 2014-15
Fund Balance—Beginning of Period	\$ (4,481.4)	\$ (2,326.5)	\$ (1,608.6)	\$ 2,527.5	\$ 4,212.0
Restatements					
Prior Year Adjustment	1,610.0	1,071.7	783.0	--	—
Fund Balance—Beginning of Period, as Restated	\$ (2,871.4)	\$ (1,254.8)	\$ (825.6)	\$ 2,527.5	\$ 4,212.0
Revenues	\$ 92,122.5	\$ 85,568.5	\$ 98,102.4	\$ 99,800.9	\$ 106,858.6
Other Financing Sources					
Transfers from Other Funds	1,661.5	1,998.6	1,812.8	346.3	(2,355.9) ^(c)
Other Additions	53.2	261.5	—	—	—
Total Revenues and Other Sources	\$ 93,837.2	\$ 87,828.6	\$ 99,915.2	\$ 100,147.2	\$ 104,502.7
Expenditures					
State Operations ^(e)	\$ 26,533.6 ^(d)	\$ 23,682.8	\$ 23,734.4	\$ 26,450.3	\$ 28,071.0
Local Assistance	65,173.1 ^(f)	63,845.2 ^(f)	73,047.0	71,819.8	76,973.7
Capital Outlay	139.5	103.1	33.8	111.2	74.1
Unclassified	—	—	(253.1)	81.4	1,674.4 ^(g)
Other Uses					
Transfer to Other Funds	401.6	551.3	— ^(h)	— ^(h)	— ^(h)
Total Expenditures and Other Uses	\$ 92,247.8	\$ 88,182.4	\$ 96,562.1	\$ 98,462.7	\$ 106,793.2
Revenues and Other Sources Over or (Under)					
Expenditures and Other Uses	\$ 1,589.4	\$ (353.8)	\$ 3,353.1	\$ 1,684.5	\$ (2,290.5)
Fund Balance					
Deferred Payroll	772.6 ⁽ⁱ⁾	752.9 ⁽ⁱ⁾			
Reserved for Encumbrances	846.6	617.9	954.6	954.6	954.6
Reserved for Unencumbered Balances of Continuing Appropriations ^(j)	1,009.0	1,685.4	—	—	—
Unreserved—Undesignated ^(k)	(4,954.7)	(4,664.8)	1,572.9	3,257.4	966.9
Fund Balance—End of Period	\$ (2,326.5)	\$ (1,608.6)	\$ 2,527.5	\$ 4,212.0	\$ 1,921.5

(Footnotes on Following Page)

- (a) These statements have been prepared on a budgetary basis in accordance with state law and some modifications would be necessary in order to comply with generally accepted accounting principles (“GAAP”). The Supplementary Information contained in the state’s Audited Basic Financial Statements for the year ended June 30, 2012, attached as APPENDIX F to this Official Statement, contains a description of the differences between the budgetary basis and the GAAP basis of accounting and a reconciliation of the June 30, 2012 fund balance between the two methods. See “FINANCIAL STATEMENTS.”
- (b) Source: Department of Finance, as of the 2014-15 Governor’s Budget.
- (c) Includes a \$1,591 million transfer to the Budget Stabilization Account (BSA) for rainy day purposes.
- (d) The Department of Conservation (“DOC”) did not submit the required year-end financial statements to the State Controller’s Office for fiscal year 2010-11 in time to be included in the Budgetary/Legal Basis Annual Report (“BLBAR”). The DOC amounts reported in the BLBAR include the June 30 cash balances, plus accruals, derived from actual activity reported through December 5, 2011 for fiscal year 2010-11.
- (e) Includes debt service on general obligation bonds. The estimated amount of debt service is \$4.9 billion and \$5.3 billion for fiscal years 2013-14 and 2014-15, respectively. These amounts are net of the federal Build America Bonds subsidy and various reimbursements to the General Fund from other funds, totaling approximately \$1.4 billion in fiscal year 2013-14 and \$1.5 billion in fiscal year 2014-15, to offset debt service costs of certain bonds. (See “STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Capital Facilities Financing – Build America Bonds.”) The 2013-14 estimated debt service includes \$201 million funded out of the UC’s budget to pay debt service costs. The 2014-15 estimated debt service includes \$193 million funded out of the UC’s budget and \$189 million funded out of the CSU’s budget to pay debt service. Debt service amounts for earlier years are set forth in the table titled “Outstanding State Debt Fiscal Years 2007-08 through 2012-13” under “STATE DEBT TABLES.”
- (f) In fiscal year 2009-10, Proposition 1A of 2004 was suspended when the Governor declared a fiscal emergency allowing the state to offset local assistance expenditures with \$1.9 billion of property tax revenue borrowed from the local governments. The state repaid the obligation, plus interest, in June 2013. In fiscal year 2010-11, \$350 million of local property tax revenues were shifted to offset state General Fund costs and in fiscal year 2011-12 another \$43 million were shifted. Fiscal year 2012-13 amounts are not yet finalized.
- (g) Includes expenditure of \$1,591 million for early repayment of the Economic Recovery Bonds.
- (h) “Transfer to Other Funds” is included either in the expenditure totals detailed above or as “Transfers from Other Funds.”
- (i) Deferred Payroll, which began with the June 2010 payroll, is on-going and represents the amount of June payroll expenses deferred to July of the following fiscal year, for all state departments paid through the uniform payroll system. The Department of Finance, pursuant to Government Code Sections 12472.5 and 13302, implements the deferrals of June payroll expenditures for various governmental and nongovernmental cost funds. Deferral amounts for fiscal years 2012-13, 2013-14 and 2014-15 are not yet available.
- (j) For purposes of determining whether the General Fund budget, in any given fiscal year, is in a surplus or deficit condition, see Chapter 1238, Statutes of 1990, amending Government Code Section 13307. As part of the amendment, the unencumbered balances of continuing appropriations which exist when no commitment for expenditure is made should be an item of disclosure, but the amount shall not be deducted from the fund balance. In accordance with Government Code Section 12460, the BLBAR reflects a specific reserve for the encumbered balance for continuing appropriations.
- (k) Both actual and estimated amounts include SFEU. The Department of Finance generally includes in its estimates of the SFEU and set aside reserves, if any, the items reported in the table under “Reserved for Unencumbered Balances of Continuing Appropriations,” and “Unreserved – Undesignated.”

Source: Actual amounts for fiscal years 2010-11 and 2011-12: State of California, Office of the State Controller
 Amounts for fiscal years 2012-13 to 2014-15: State of California, Department of Finance.

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The following table contains certain summary information concerning major General Fund revenue sources for an eight-year period:

TABLE 5
General Fund Revenues and Transfers

(Dollars in Thousands)

Fiscal Year	Sales & Use Tax	Personal Income Tax	Corporate Income Tax	Other Revenues and Transfers	Total
2007-08	\$26,613,264	\$54,181,857	\$11,849,097	\$9,877,663	\$102,521,881
2008-09	23,753,364	43,375,959	9,535,679	6,107,110	82,772,112
2009-10	26,740,781	44,852,331	9,114,589	6,337,891	87,045,592
2010-11	26,983,000	49,445,469	9,613,594	7,401,213	93,443,276
2011-12	18,658,000 ^(a)	54,261,266 ^{(b)(d)}	7,233,000	6,633,378 ^(c)	86,785,644
2012-13 ^(e)	20,482,000 ^(d)	65,332,000 ^(d)	7,462,000 ^(f)	6,639,162	99,915,162
2013-14 ^(e)	22,920,000 ^(d)	64,287,000 ^{(d)(g)}	7,971,000 ^{(f)(g)}	4,969,233	100,147,233
2014-15 ^(e)	24,071,000 ^{(d)(g)}	69,764,000 ^{(d)(g)}	8,682,000 ^{(f)(g)}	1,985,705 ^(h)	104,502,705

^(a) Reflects a decrease in the Sales & Use Tax rate from 6 percent to 5 percent (rate was temporarily increased from 5 percent to 6 percent from April 1, 2009 through June 30, 2011) and realignment of revenues related to shifting 1.0625 percent of the Sales & Use Tax rate to the Local Revenue Fund 2011. These two changes decrease General Fund revenues by roughly \$10 billion annually.

^(b) Reflects the expiration of a temporary 0.25 percent surcharge and the reduced dependent exemption credit for the 2009 and 2010 tax years. These two changes decrease General Fund revenues by an estimated \$3.537 billion in fiscal year 2011-12.

^(c) Reflects the expiration of a temporary 0.5 percent increase in the vehicle license fee rate (rate was increased from 0.65 percent to 1.15 percent, effective May 19, 2009 through June 30, 2011), decreasing General Fund revenues by an estimated \$1.330 billion in fiscal year 2011-12.

^(d) Reflects the passage of Proposition 30, The Schools and Local Public Safety Protection Act of 2012, which temporarily increases tax rates on the highest income Californians, and temporarily increases the sales and use tax rate by 0.25 percent. Since higher personal income tax rate applies to income received in 2012, a majority of the expected new revenue for that year is allocated to fiscal year 2011-12, although the cash receipts did not begin occurring until December 2012.

^(e) Estimated.

^(f) Reflects the passage of Proposition 39, which requires single sales factor apportionment for most multi-state businesses. See "STATE FINANCES – Sources of Tax Revenue – Corporation Tax" for a discussion of recent difficulties in projecting corporation tax receipts.

^(g) Reflects the enactment of the Economic Development Initiative pursuant to Chapters 69 and 70, Statutes of 2013, which reformed California's economic development programs by replacing them with three tax incentive programs: (1) a new hiring credit, (2) a sales tax exemption for manufacturing or biotech research and development equipment purchases, and (3) a business tax credit in exchange for investment and employment expansion in California.

^(h) Includes transfer of \$1,591 million from the General Fund to the Budget Stabilization Account for rainy day purposes.

Source: State of California, Department of Finance.

Revenue and Expenditure Assumptions

The table below presents the Department of Finance's budget basis statements of General Fund revenue sources and expenditures by function for fiscal years 2012-13 through 2014-15, as set forth in the 2014-15 Governor's Budget.

TABLE 6
General Fund Revenue by Sources and Expenditures
Fiscal Years 2012-13 through 2014-15
(Dollars in Millions)

Revenues	2012-13 Actual (as of January 2014)	2013-14 Revised (as of January 2014)	2014-15 Proposed (as of January 2014)
Source			
Personal Income Tax	\$ 65,332	\$ 64,287	\$ 69,764
Sales and Use Tax	20,482	22,920	24,071
Corporation Tax	7,462	7,971	8,682
Insurance Tax	2,221	2,143	2,297
Alcoholic Beverage Taxes and Fees	357	350	357
Cigarette Tax	90	89	86
Motor Vehicle Fees	26	20	20
Other ^(a)	3,945	2,367	817
Subtotal	\$ 99,915	\$ 100,147	\$ 106,094
Transfer to the Budget Stabilization Account/Rainy Day Fund	0	0	-1,591
Total	\$ 99,915	\$ 100,147	\$ 104,503

Expenditures	2012-13 Actual	2013-14 Revised	2014-15 Proposed
Function			
Legislative, Judicial and Executive	\$ 1,930	2,694	2,844
State and Consumer Services ^(b)	0	0	0
Business, Transportation & Housing ^(b)	0	0	0
Business, Consumer Services & Housing ^(c)	215	646	745
Transportation ^(c)	-31 ^(d)	151	212
Natural Resources	2,096	2,127	2,175
Environmental Protection	46	47	54
Health and Human Services	26,732	28,330	28,793
Corrections and Rehabilitation	8,613	9,361	9,560
K-12 Education	42,484	41,333	45,251
Higher Education	10,041	11,173	12,377
Labor and Workforce Development	344	298	268
Government Operations ^(c)	641	753	685
General Government			
Non-Agency Departments	429	519	610
Tax Relief/Local Government	2,527	420	437
Statewide Expenditures	495	611	1,191
Supplemental Payment to the Economic Recovery Bonds	0	0	1,591
Total Expenditures	\$ 96,562	\$ 98,463	\$ 106,793

^(a) Generally consists of transfers and loans, and various smaller amounts for miscellaneous fees, taxes, royalties, tribal gaming revenues, unclaimed property and other sources.

^(b) These agencies were eliminated as part of the Governor's Reorganization Plan 2, effective July 1, 2013. The departments or programs within these agencies have been moved to other agencies. For comparative purposes, the 2012-13 actual expenditures are reported based on the new organizational structure.

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- (c) These agencies were created as part of the Governor's Reorganization Plan 2, effective July 1, 2013. They include departments or programs from the eliminated agencies or other agencies. Although these agencies were created after 2012-13, for comparative purposes, actual 2012-13 expenditures are reported based on the new organizational structure.
- (d) The use of certain transportation funds to offset General Fund costs for general obligation bond debt service exceeded other program costs for fiscal year 2012-13 and resulted in a net General Fund savings.

Source: State of California, Department of Finance. Figures in this table may differ from the figures in Table 16; see "Note" to Table 16.

Cap and Trade Program

The Cap and Trade program is a key element in the state's climate plan. It sets a statewide limit on the sources of greenhouse gases ("GHG") responsible for 85 percent of California GHG emissions. In fiscal year 2012-13, the California Air Resources Board ("CARB") began auctioning GHG emission allowances as a market-based compliance mechanism authorized by the California Global Warming Solutions Act, Chapter 488, Statutes of 2006 ("AB 32").

CARB has held six auctions through February, 2014, which generated \$663 million in allowance proceeds to the Greenhouse Gas Reduction Fund. The remaining auction for 2013-14 will occur in May 2014. Currently, GHG emissions from electricity and large industrial sources are subject to the cap.

The 2013 Budget Act included a one-time General Fund loan of \$500 million from Cap and Trade auction proceeds. The 2014-15 Governor's Budget proposes \$850 million of expenditures from the Greenhouse Gas Reduction Fund for programs that reduce GHG emissions. This amount of resources includes repayment of \$100 million of the 2013 Budget Act loan, with the remaining balance being repaid with interest immediately when needed to meet the future needs of the GGR Fund, or by the end of 2017-18, whichever occurs sooner.

Legal challenges to the authority of CARB to conduct auctions under the state's cap and trade program allege the auction revenues are an unconstitutional tax under the state Constitution. See "LITIGATION – Action Challenging Cap and Trade Program Auctions."

DEFERRED OBLIGATIONS

Despite eliminating the structural deficit and maintaining a balanced budget over the last three budgets, the state continues to face major long-term challenges and must continue to address the consequences of budget-balancing actions taken in the past. As part of the 2014-15 Governor's Budget projection, the Administration prepared a table showing \$24.9 billion in "budgetary borrowing" or "deferred obligations" as of June 30, 2014 based on 2013 Budget Act policies, which consisted of budget solutions adopted over the prior decade which had the effect of pushing costs into the recent and future years. (These obligations are presented in the second column of Table 7 below.) Table 7 represents a point-in-time estimate of what budgetary borrowings were at the end of fiscal year 2010-11, subsequent projections and a plan to pay off the remaining amounts by the end of fiscal year 2017-18. In addition to the amount provided in

the 2013-14 Budget Act, the 2014-15 Governor's Budget provides \$4.3 billion in payments allocated to 2013-14 and previous fiscal years to accelerate the pay down of deferred obligations. The projections are based on a variety of assumptions, including assumptions concerning economic conditions, and state revenues and expenditures. Actual conditions may differ materially from the assumptions, and there can be no assurances the projections will be achieved.

Items listed in Table 7 as "deferrals" or "deferred payments" represent actions taken to move required payments from one fiscal year into the next fiscal year for budgetary savings. These deferrals end up being repeated year after year to avoid having to make a double payment within a fiscal year until they are repaid, and such a double payment occurs. The deferred obligations shown in Table 7 are a portion of Proposition 98 payments to schools and community colleges, certain Medi-Cal reimbursements, one month's state payroll, and the final quarterly payment to the state pension fund. Other budgetary borrowings shown in Table 7 are repayment of the ERBs which financed budget deficits from prior to fiscal year 2003-04, repayment of certain legislatively approved interfund borrowings, reimbursement of borrowings from state funds and local governments, reimbursements to local governments and school districts for the costs of state mandates placed on those entities under state laws, and repayments to school and community college districts of amounts owed under Proposition 98 from recalculation of the guarantee after the end of a fiscal year, referred to in Table 7 as "underfunding of Proposition 98" and referred to elsewhere in this APPENDIX A as "settle-up payments."

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All of the outstanding budgetary borrowing and deferrals shown in Table 7 would be repaid by the end of fiscal year 2017-18.

TABLE 7
Deferred Obligations
2014-15 Governor's Budget

(Dollars in Millions)

	Outstanding (as of end of 2010-11)	Outstanding (as of end of 2013-14 based upon 2013 Budget Act policies)	Proposed Supplement al Payments to 2013-14 and Earlier	Projected Repayments				Remaining Amount at June 30, 2018
				2014-15	2015-16	2016-17	2017-18	
Deferred Payments to Schools and Community Colleges	\$10,430	\$6,164	\$3,690	\$2,474	\$0	\$0	\$0	\$0
Economic Recovery Bonds ^(a)	7,100	3,914	0	3,165	0	0	0	0
Loans from Special Funds	5,100	3,880	0	927	2,021	932	0	0
Unpaid Costs to Local Governments, Schools and Community Colleges for State Mandates	4,300	5,382	0	0	1,993	1,752	1,637	0
Underfunding of Proposition 98	3,000	2,391 ^(b)	598	0	1,793	0	0	0
Borrowing from local government (Proposition 1A of 2004)	1,900	0	0	0	0	0	0	0
Deferred Medi-Cal Costs	1,200	1,773	0	60	40	0	1,673	0
Deferral of State Payroll Costs from June to July	759	783	0	0	0	783	0	0
Deferred Payments to CalPERS	524	411	0	0	0	411	0	0
Borrowing from Transportation Funds (Proposition 42)	417	168	0	83	85	0	0	0
Total	\$34,730	\$24,866	\$4,288	\$6,709	\$5,932	\$3,878	\$3,310	\$0

^(a) The annual values reflect the amounts needed to backfill the Proposition 98 budget (rather than the reduction in the outstanding principal amount of Economic Recovery Bonds). The Economic Recovery Bonds are expected to be effectively paid off by June 30, 2015, including use of \$1.6 billion transferred from the BSA as a supplemental payment towards the Economic Recovery Bonds. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Economic Recovery Bonds."

^(b) The amount reflects the Proposition 98 settle-up obligations detailed in Table 20, plus the \$274 million balance of the settlement agreement in *Williams, et al., v. State of California, et al.*

Source: Department of Finance

In some instances, such as the ERBs, the repayment mechanism over time is included in annual budgets. In other cases, such as the loans from special funds, the repayment mechanism remains within the discretion of the Legislature. The Administration's plan is to completely pay off the "wall of debt" before the termination of the temporary additional personal income tax rates under Proposition 30 on December 31, 2018. Assuming continued economic growth and responsible fiscal policies, the Administration believes the state will be able to maintain positive structural fiscal balances past the period of the Proposition 30 temporary taxes.

As stated earlier in this APPENDIX A, the Department of Finance estimates that over \$11 billion of these outstanding Deferred Obligations will be reduced by the end of 2014-15 pursuant to the Governor's Budget plan. This consists of the following items:

\$6.2 billion repayment of deferrals from schools and community colleges

\$3.2 billion from repayments or creation of escrow accounts to repay Economic Recovery Bonds

\$0.9 billion in Special Fund loan repayments

\$0.6 billion in repayments of Underfunding of Proposition 98

\$83 million in repayment of borrowing from Transportation Funds

\$60 million in repayment of deferred Medi-Cal costs

In addition to the budgetary borrowing shown in Table 7, the state faces future obligations to employees for compensated absences, costs for self-insurance, and future payment of interest owed on borrowings from the federal government for unemployment insurance payments. See “STATE FINANCES – Unemployment Insurance” below. Further, in addition to the Proposition 98 deferred payment and underfunding shown in Table 7, there is another obligation owed under Proposition 98 which arises when under the terms of Proposition 98 there is an underfunding, such as a suspension of the guarantee, which is called a “maintenance factor.” The Department of Finance estimates that the total outstanding balance of Proposition 98 maintenance factor payments would be \$7.9 billion at the end of fiscal year 2013-14. The outstanding balance projected at the end of fiscal year 2014-15 will be \$4.5 billion, reflecting a year-over-year decrease in the Proposition 98 maintenance factor balance due to the inclusion of a maintenance factor repayment in the calculation of the Proposition 98 funding level in fiscal year 2014-15. The Proposition 98 maintenance factor is repaid pursuant to the constitutional repayment formula in years when growth in per capita General Fund outpaces growth in per capita income. See “STATE FINANCES – Proposition 98 and K-14 Funding.”

The two main retirement systems managed by state entities, CalPERS and CalSTRS, each have substantial unfunded liabilities. See “PENSION TRUSTS.” The state also has a substantial unfunded liability relating to state employee retirees’ postemployment healthcare benefits. See “STATE FINANCES – Retiree Health Care Costs.” In addition, the state has \$33.45 billion of authorized and unissued long-term bonds. See “STATE INDEBTEDNESS AND OTHER OBLIGATIONS.”

CASH MANAGEMENT

Cash Management Tools

General. The majority of the state’s General Fund receipts are received in the latter part of the fiscal year. Disbursements from the General Fund occur more evenly throughout the fiscal year. The state’s cash management program customarily addresses this timing difference by making use of internal borrowing (see “– Internal Borrowing”) and by issuing short-term notes in the capital markets (see “– External Borrowing”). External borrowing is typically done with RANs that are payable not later than the last day of the fiscal year in which they are issued. RANs have been issued in all but one fiscal year since the mid-1980s and have always been paid

at maturity. The state also is authorized under certain circumstances to issue RAWs that are payable in the succeeding fiscal year. The state issued RAWs to bridge short-term cash management shortages in 1992, 1993, 1994, 2002 and 2003. See “STATE FINANCES – State Warrants – Reimbursement Warrants” for more information on RAWs.

RANs and RAWs are both payable from any “Unapplied Money” in the General Fund of the state on their maturity date, subject to the prior application of such money in the General Fund to pay Priority Payments. “Priority Payments” consist of: (i) the setting apart of state revenues in support of the public school system and public institutions of higher education (as provided in Section 8 of Article XVI of the state Constitution); (ii) payment of the principal of and interest on general obligation bonds and general obligation commercial paper notes of the state as and when due; (iii) reimbursement from the General Fund to any special fund or account to the extent such reimbursement is legally required to be made to repay borrowings therefrom pursuant to California Government Code Sections 16310 or 16418; and (iv) payment of state employees’ wages and benefits, state payments to pension and other state employee benefit trust funds, state Medi-Cal claims, lease payments to support lease-revenue bonds, and any amounts determined by a court of competent jurisdiction to be required by federal law or the state Constitution to be paid with state warrants that can be cashed immediately. See “STATE FINANCES – State Warrants.”

The state has employed additional cash management measures during some fiscal years; all of the following techniques were used at one time or another during the last several fiscal years and some of them are expected to be utilized in the current fiscal year:

The State Controller has delayed certain types of disbursements from the General Fund.

Legislation was enacted in each of the last several fiscal years increasing the state’s internal borrowing capability, and the state has increased the General Fund’s internal borrowings. See “STATE FINANCES – Inter-Fund Borrowings.”

Legislation has been enacted deferring some of the state’s disbursements until later in the then-current fiscal year, when more cash receipts are expected.

The issuance of registered warrants (commonly referred to as “IOUs”) because of insufficient cash resources (last occurred in 2009). (See “STATE FINANCES – State Warrants” for an explanation of registered warrants.)

Legislation was enacted in fiscal year 2011-12 to increase borrowable resources through creation of the State Agency Investment Fund (“SAIF”) to allow state entities whose monies are not required by law to be deposited in the Pooled Money Investment Account (“PMIA”), to make deposits of at least \$500 million into this new borrowable fund within the PMIA. The California State University and University of California systems deposited a total of \$1.7 billion into the SAIF on September 26, 2011, which remained on deposit until April 2013.

Legislation was enacted in the 2012-13 Budget to establish a Voluntary Investment Fund (the “VIP Fund”), similar to the SAIF, to allow for local governmental entities to make deposits of at least \$200 million in the PMIA. The VIP Fund has not been used to date and it is not part of the state’s current cash management plans, but it could be utilized in the future if the state faces cash flow shortfalls.

Internal Borrowing. The General Fund is currently authorized by law to borrow for cash management purposes from more than 700 of the state’s approximately 1,300 other funds in the State Treasury (the “Special Funds”). Total borrowing from Special Funds must be approved by the Pooled Money Investment Board (“PMIB”). The State Controller submits an authorization request to the PMIB quarterly, based on forecasted available funds and borrowing needs. The Legislature may from time to time adopt legislation establishing additional authority to borrow from Special Funds. On February 3, 2012, the Governor signed SB 95 (Chapter 1, Statutes of 2012, “SB 95”), a statute which clarified that certain transportation funds and other funds were available for short-term cash management borrowing, which provided an estimated \$865 million of additional capacity at certain times of the year. The state has historically made extensive use of its internal borrowing capability to provide cash resources to the General Fund. The PMIB has authorized the internal borrowing of up to \$21.999 billion for the period ending March 31, 2014.

One fund from which moneys may be borrowed to provide additional cash resources to the General Fund is the BSA, a reserve fund established in 2004 by Proposition 58. However, during fiscal years 2008-09 to 2013-14, there were no funds available in the BSA. The BSA will be funded at an estimated \$1.591 billion in fiscal year 2014-15. See “STATE FINANCES – Budget Reserves – Budget Stabilization Account.” The state also may transfer funds into the General Fund from the state’s SFEU, which is not a Special Fund. See “STATE FINANCES – Inter-Fund Borrowings” for a further description of this process.

External Borrowing. As noted above, issuance of RANs is a normal part of the state’s annual cash management program. The state issued \$10 billion of RANs on August 23, 2012 which were all repaid when due. The state issued \$5.5 billion of RANs to assist in cash management for fiscal year 2013-14. See “STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Cash Management Borrowings.”

Payment Deferrals. From time to time, the Legislature changes by statute the due date for various payments, including those owed to public schools, universities and local governments, until a later date in the fiscal year in order to more closely align the state’s revenues with its expenditures. This technique has been used several times in the last few fiscal years and is being used this fiscal year. Some of these statutory deferrals were made permanent, and others were implemented only for one fiscal year.

In addition, state law gives the State Controller some flexibility as to how quickly the state must pay its bills. For instance, income tax refunds for personal income taxes are not legally due until 45 days after the return filing deadline, which is normally April 15. Accordingly, while the state has typically paid tax refunds as returns are filed, it can conserve cash by withholding refund payments until after the April 15 due date. Payments to vendors generally must be made within 45 days of receipt of an invoice. The state may delay payment

until the end of this period, or it may even choose to make these payments later and pay interest. These delays are only used if the State Controller foresees a relatively short-term cash flow shortage.

Cash Management in Fiscal Year 2012-13

For the second consecutive year, the state entered the fiscal year in a stronger cash position than it had in some prior years. Timely enactment of the 2012 Budget Act allowed the state to carry out its regular cash management borrowing with RANs early in the year, and without the need for Interim RANs for the first time in three years. The state issued \$10 billion of RANs on August 23, 2012.

The Legislature enacted a cash management bill which authorized deferral of certain payments during fiscal year 2012-13, including payments to K-12 schools (not to exceed \$2.5 billion in the aggregate at any one time), reimbursements to the federal government for certain social service costs, payments to certain local government social services, transportation payments and Proposition 63 mental health payments (not to exceed \$1 billion in the aggregate at one time), higher education payments, CalSTRS payment modifications and trial operations (not including payroll). The deferrals were made as planned in July and October of 2012. On November 21, 2012, the State Controller, State Treasurer and Director of Finance jointly determined that there would be sufficient cash in the General Fund to repay these deferrals one month early in December 2012. The officials subsequently determined that the March 2013 deferrals authorized by the cash management bill would not be necessary.

The state continued to benefit from \$1.7 billion of additional internal borrowable resources in the SAIF until they were returned in late April 2013. The Legislature created a VIP Fund, described above, which could provide additional short-term cash management borrowing resources, but there are no current plans for use of this fund.

Cash Management in Fiscal Year 2013-14

The state's cash management plan in fiscal year 2013-14 consists primarily of internal borrowing from special funds and issuance of revenue anticipation notes in the amount of \$5.5 billion. In addition, pursuant to legislation enacted in the last fiscal year, within fiscal year 2013-14 a payment of \$250 million to the California State University ("CSU") and a payment of \$500 million to the University of California are planned to be deferred. Such deferrals are at the discretion of the Director of Finance and shall be repaid in May or June of 2014. The CSU has agreed that in lieu of a payment deferral it will deposit a like amount into a fund in the State Treasury which can be borrowed by the General Fund.

State fiscal officers constantly monitor the state's cash position and if it appears that cash resources may become inadequate (including the maintenance of a projected cash reserve of at least \$2.5 billion at any time), they will consider the use of other cash management techniques as described above, including seeking additional legislation.

STATE INDEBTEDNESS AND OTHER OBLIGATIONS

General

The State Treasurer is responsible for the sale of most debt obligations of the state and its various authorities and agencies. The state has always paid when due the principal of and interest on its general obligation bonds, general obligation commercial paper notes, lease-revenue obligations and short-term obligations, including RANs and RAWs. Additional information regarding the state's long-term debt appears in the section "STATE DEBT TABLES."

Capital Facilities Financing

General Obligation Bonds

The state Constitution prohibits the creation of general obligation indebtedness of the state unless a bond measure is approved by a majority of the electorate voting at a general election or a direct primary. Each general obligation bond act provides a continuing appropriation from the General Fund of amounts for the payment of debt service on the related general obligation bonds, subject only to the prior application of moneys in the General Fund to the support of the public school system and public institutions of higher education. Under the state Constitution, appropriations to pay debt service on any general obligation bonds cannot be repealed until the principal and interest on such bonds have been paid. See "STATE FINANCES – State Expenditures." Certain general obligation bond programs, called "self-liquidating bonds," receive revenues from specified sources so that moneys from the General Fund are not expected to be needed to pay debt service, but the General Fund will pay the debt service, pursuant to the continuing appropriation contained in the bond act, if the specified revenue source is not sufficient. The principal self-liquidating bond programs are the ERBs, supported by a special sales tax, and veterans general obligation bonds, supported by mortgage repayments from housing loans made to military veterans. See "– Economic Recovery Bonds."

General obligation bonds are typically authorized for infrastructure and other capital improvements at the state and local level. Pursuant to the state Constitution, general obligation bonds cannot be used to finance state budget deficits (except as already authorized by ERBs, as described below).

As of February 1, 2014, the state had outstanding \$80,519,520,000 aggregate principal amount of long-term general obligation bonds, of which \$75,186,850,000 were payable primarily from the state's General Fund, and \$5,332,670,000 were "self-liquidating" bonds payable first from other special revenue funds. As of February 1, 2014, there were unused voter authorizations for the future issuance of \$28,285,236,000 of long-term general obligation bonds, some of which may first be issued as commercial paper notes (see "General Obligation Commercial Paper Program" below). Of this unissued amount, \$706,210,000 is for general obligation bonds payable first from other revenue sources. See the table "Authorized and Outstanding General Obligation Bonds" following the caption "STATE DEBT TABLES."

The Legislature has placed on the statewide election ballot on June 3, 2014 a measure to approve \$600 million of general obligation bonds to finance rental housing programs for military

veterans. This measure also cancelled \$600 million of existing authorization from a 2008 veterans home ownership bond act, which is payable primarily from mortgage payments made by veteran homeowners. A ballot measure is scheduled to be submitted to the voters at the statewide election in November 2014 (rescheduled from 2012) to approve the issuance of \$11.14 billion in general obligation bonds for a wide variety of purposes relating to improvement of California's water supply systems, drought relief, and groundwater protection. Additional bond measures may be included on future election ballots, but any proposed bond measure must first be approved by a 2/3 vote of the Legislature or placed on the ballot through the initiative process.

Variable Rate General Obligation Bonds

The general obligation bond law permits the state to issue as variable rate indebtedness up to 20 percent of the aggregate amount of long-term general obligation bonds outstanding. These bonds are described generally in the following table and represent about 5.0 percent of the state's total outstanding general obligation bonds. With respect to the \$850,000,000 of variable rate general obligation bonds having mandatory tender dates, if these bonds cannot be remarketed on their respective scheduled mandatory tender dates, there is no default but the interest rate on the series of such bonds not remarketed on such date would be increased in installments thereafter until such bonds can be remarketed or refunded, ultimately reaching either 11 percent on the 181st day or 10 percent on the 180th day, as applicable. Furthermore, with respect to the \$100,000,000 of these bonds with a mandatory tender date of May 1, 2015, until such bonds are remarketed or refunded, they will be subject to quarterly mandatory redemptions of \$5 million each over a period of five years commencing six months after the initial unsuccessful remarketing.

Type of Bonds	Outstanding Principal Amount (\$000) as of February 1, 2014	Current Variable Rate Interest Mode	Liquidity Support^(a)	Other Information
General Obligation	\$2,473,690	Daily/Weekly VRDO	Letters of Credit	
General Obligation	400,000	Indexed Floating Rate to Respective Mandatory Tender Dates	None	Mandatory Tenders on May 1, 2015, December 1, 2016, December 1, 2017, December 3, 2018
General Obligation	98,100	Indexed Floating Rate to Respective Maturity Dates	None	Fixed Maturities on each May 1 in the years 2017 through 2020
General Obligation	450,000	Fixed Term Rate to Respective Mandatory Tender Dates	None	Mandatory Tenders on December 1, 2016 and December 1, 2017
ERBs	110,370	Daily VRDO	Letter of Credit	Letter of Credit expires June 13, 2014 ^(b)
ERBs	<u>500,000</u>	Fixed Term Rate to Mandatory Tender Date	None	Mandatory Tender on July 1, 2014 ^(c)
TOTAL	\$4,032,160			

^(a) See "Bank Arrangements."

^(b) Expected to be redeemed by fall 2014.

^(c) Expected to be redeemed on that date.

Source: State of California, Office of the State Treasurer

Under state law, except for the ERBs, certain mandatory tender bonds and certain indexed floating rate bonds without credit enhancement, the state must pay the principal and interest of any general obligation bonds which are subject to optional or mandatory tender, and which are not remarketed or, if applicable, purchased by financial institutions which provide liquidity support to the state. The state has not entered into any interest rate hedging contracts in relation to any of its variable rate general obligation bonds. The state has no auction rate bonds outstanding.

General Obligation Commercial Paper Program

Pursuant to legislation enacted in 1995, voter-approved general obligation indebtedness may be issued either as long-term bonds or, for some but not all bond issues, as commercial paper notes. Commercial paper notes may be renewed or may be refunded by the issuance of long-term bonds. It is currently the state's policy to use commercial paper notes to provide flexibility for bond programs, such as to provide interim funding of voter-approved projects and to facilitate refunding of variable rate bonds into fixed rate bonds. Commercial paper notes are not included in the calculation of permitted variable rate indebtedness described under "Variable Rate General Obligation Bonds" and are not included in the figures provided above in the section "General Obligation Bonds." A total of \$1.725 billion in principal amount of commercial paper notes is now authorized under agreements with various banks. See the "BANK ARRANGEMENTS" table for a list of the credit agreements supporting the commercial paper program. As of March 3, 2014, there was \$892,325,000 principal amount of commercial paper notes outstanding.

Enhanced Transportation Bonds

"Self-liquidating" general obligation bonds have a dedicated revenue source which is expected to pay all of the debt service, but if the revenue source is for some reason insufficient, the General Fund pays the debt service on the same priority level as all other general obligation bonds. In 2013 the Legislature enacted a bill (Chapter 35, Statutes of 2013, "SB 85") which created an additional "self-liquidating" general obligation bond, similar to Veterans Bonds (which use mortgage repayments) and ERBs (dedicated sales tax). The new program, called "Enhanced Transportation Bonds," uses Vehicle Weight Fees ("VWF") charged on commercial trucks and vans to pay the debt service on certain general obligation bonds for transportation purposes previously approved by voters in 2006, with the state's general obligation pledge as a secondary source of payment. VWF are an excise tax, not part of the General Fund, and have totaled about \$900 million to \$1 billion per year in the recent past, although there can be no assurance of future VWF amounts. Under the law prior to enactment of SB 85, VWF moneys were transferred to the General Fund to offset the debt service costs of transportation bonds; SB 85 reversed the order in which funds are used. The state intends to start issuing Enhanced Transportation Bonds in the fall of 2014. Before any issuance of Enhanced Transportation Bonds, the State Treasurer must determine that for a period of twelve consecutive months out of the previous eighteen months, the total amount of VWF received is equal to at least two times the maximum annual debt service on all Enhanced Transportation Bonds, including the bonds proposed to be issued. The new program under SB 85 will not have any effect on any general obligation transportation bonds already issued.

Bank Arrangements

In connection with the letters of credit obtained by the state in connection with variable rate demand obligations (“VRDOs”) and the commercial paper program (“CP”), the state has entered into a number of reimbursement agreements or other credit agreements with a variety of financial institutions as set forth in the table titled “BANK ARRANGEMENTS” which immediately follows the end of the text of this APPENDIX A, prior to “STATE DEBT TABLES.” These agreements include various representations and covenants of the state, and the terms (including interest rates and repayment schedules) by which the state would be required to repay any drawings (including drawings resulting from any failed remarketings) on the respective letters of credit or other credit enhancement to which such credit agreements relate. To the extent that VRDOs or CP cannot be remarketed over an extended period (whether due to reductions in the credit ratings of the institution providing credit enhancement or other factors), interest payable by the state pursuant to the reimbursement agreement or credit agreement would generally increase over current market levels relating to the VRDOs or CP, and the principal repayment period would generally be shorter (typically less than five years) than the repayment period otherwise applicable to the VRDOs or CP. On occasion the state’s VRDOs or CP were not remarketed resulting in draws on the applicable credit facilities, but this has not occurred since 2009.

Lease-Revenue Obligations

In addition to general obligation bonds, the state has acquired and constructed capital facilities through the use of lease-revenue borrowing (also referred to as lease-purchase borrowing). Such borrowing must be authorized by the Legislature in a separate act or appropriation. Under these arrangements, the SPWB, another state or local agency or a joint powers authority issued bonds to pay for the acquisition or construction of facilities such as office buildings, university buildings, courthouses or correctional institutions. These facilities are leased to a state agency, the California State University or the Judicial Council under a long-term lease that provides the source of payment of the debt service on the lease-revenue bonds. In some cases, there was not a separate bond issue, but a trustee directly created certificates of participation in the state’s lease obligation, which were then marketed to investors. Under applicable court decisions, such lease arrangements do not constitute the creation of “indebtedness” within the meaning of the state constitutional provisions that require voter approval. For purposes of this APPENDIX A and the tables under “STATE DEBT TABLES,” the terms “lease-revenue obligation,” “lease-revenue financing,” “lease-purchase obligation” or “lease-purchase” mean principally bonds or certificates of participation for capital facilities where the lease payments providing the security are payable from the operating budget of the respective lessees, which are primarily, but not exclusively, derived from the General Fund. The state had \$10,235,955,000 in lease-revenue obligations outstanding as of February 1, 2014. The tables under “STATE DEBT TABLES” do not include equipment leases or leases which were not sold, directly or indirectly, to the public capital markets. The SPWB, which is authorized to sell lease-revenue bonds, had approximately \$5.87 billion of authorized and unissued bonds as of February 1, 2014.

Non-Recourse Debt

Certain state agencies and authorities issue revenue obligations for which the General Fund has no liability. These revenue bonds represent obligations payable from state revenue-producing enterprises and projects, and conduit obligations payable from revenues paid by private users or local governments of facilities financed by the revenue bonds. In each case, such revenue bonds are not payable from the General Fund. The enterprises and projects include transportation projects, various public works projects, public and private educational facilities (including the California State University and University of California systems), housing, health facilities and pollution control facilities. State agencies and authorities had approximately \$55.6 billion aggregate principal amount of revenue bonds and notes which are non-recourse to the General Fund outstanding as of June 30, 2013, as further described in the table "State Agency Revenue Bonds and Conduit Financing" under "STATE DEBT TABLES."

Build America Bonds

In February 2009, Congress enacted certain new municipal bond provisions as part of the federal economic stimulus act ("ARRA"), which allowed municipal issuers such as the state to issue "Build America Bonds" ("BABs") for new infrastructure investments. BABs are bonds whose interest is subject to federal income tax, but pursuant to ARRA the U.S. Treasury was to repay the issuer an amount equal to 35 percent of the interest cost on any BABs issued during 2009 and 2010. The BAB subsidy payments related to general obligation bonds are General Fund revenues to the state, while subsidy payments related to SPWB lease-revenue bonds are deposited into a fund which is made available to the SPWB for any lawful purpose. In neither instance are the subsidy payments specifically pledged to repayment of the BABs to which they relate. The cash subsidy payment with respect to the BABs, to which the state is entitled, is treated by the Internal Revenue Service ("IRS") as a refund of a tax credit and such refund may be offset by the Department of the Treasury by any liability of the state payable to the federal government. None of the state's BAB subsidy payments to date have been reduced because of such an offset.

Between April 2009 and December 2010, the state issued \$13.54 billion of BAB general obligation ("GO") bonds and the SPWB issued \$551 million of BAB lease-revenue bonds. \$149.62 million of the SPWB BABs were redeemed in November 2013. The aggregate amount of the subsidy payments to be received from fiscal year 2013-14 through the maturity of these bonds (mostly 20 to 30 years) based on the 35% rate is approximately \$8.3 billion for the general obligation BABs and \$223 million for the SPWB lease-revenue BABs.

Pursuant to certain federal budget legislation adopted in August 2011, starting as of March 1, 2013, the government's BAB subsidy payments were reduced as part of a government-wide "sequestration" of many program expenditures. The reduction of the BAB subsidy payment is presently scheduled to continue until 2024, although Congress can terminate or modify it sooner, or extend it. Each BAB subsidy payment was reduced by 8.7 percent for the federal 2013 fiscal year (ended September 30, 2013). This resulted in a reduction of approximately \$15.65 million from the \$367.40 million of total subsidies the state had been scheduled to receive between October 1, 2012 and September 30, 2013 for both GO and SPWB BABs. The IRS has announced that the sequestration reduction for federal 2014 fiscal year

(starting October 1, 2013) will be 7.2 percent, resulting in a reduction of approximately \$26.20 million in subsidies from a total of \$363.86 million expected to be received during that period. (The sequestration percentage is recalculated for each fiscal year.) None of the BAB subsidy payments are pledged to pay debt service, so this reduction will not affect the state's ability to pay all of its GO and SPWB BABs on time, nor have any material impact on the state's General Fund.

Future Issuance Plans; General Fund Debt Ratio

Since 2006, a significant amount of new general obligation bonds and lease revenue bonds have been authorized by voters and/or the Legislature. These authorizations led to a substantial increase in the amount of General Fund supported debt outstanding, from \$44.85 billion as of July 1, 2006 to \$85.42 billion as of February 1, 2014, while still leaving current authorized and unissued bonds of about \$33.45 billion.

In calendar years 2009 and 2010, over \$35.07 billion of new money general obligation bonds, lease-revenue bonds and Proposition 1A bonds were sold. Following the record bond issuance levels in these years, bond issuance for new money general obligation bonds has substantially decreased as funding needs have declined and departments work to manage their existing bond cash balances. In calendar year 2013, \$6.04 billion of new money general obligation and lease revenue bonds were sold, and \$4.42 billion of refunding general obligation and lease revenue bonds were sold.

Based on estimates from the 2014-15 Governor's Budget as well as updates from the Department of Finance, approximately \$4.48 billion of new money general obligation bonds (some of which may initially be in the form of commercial paper notes) and approximately \$1.41 billion of lease-revenue bonds will be issued in calendar year 2014. These estimates will be updated by the State Treasurer's office based on information provided by the Department of Finance with respect to the updated funding needs of, and actual spending by, departments. In addition, the actual amount of bonds sold will depend on other factors such as overall budget constraints, market conditions and other considerations. The state also expects to issue refunding bonds as market conditions warrant.

The ratio of debt service on general obligation and lease-revenue bonds supported by the General Fund to annual General Fund revenues and transfers (the "General Fund Debt Ratio") can be expected to fluctuate from year to year. As assumptions for future debt issuance and revenue projections are updated from time to time, any changes to these amounts will impact the projected General Fund Debt Ratio. Based on the revenue estimates contained in the 2014-15 Governor's Budget and bond issuance estimates referred to in the preceding paragraph, the General Fund Debt Ratio is estimated to equal approximately 7.46 percent in fiscal year 2013-14 and 7.43 percent in fiscal year 2014-15.

The General Fund Debt Ratio is calculated based on actual gross debt service, without adjusting for receipts from the U.S. Treasury for the state's current outstanding general obligation and SPWB lease revenue BABs or the availability of any special funds that may be used to pay a portion of the debt service to help reduce General Fund costs. The total of these offsets for general obligation bond and lease revenue debt service is estimated to equal

approximately \$1.39 billion for fiscal year 2013-14 and \$1.46 billion for fiscal year 2014-15. Including the estimated offsets reduces the General Fund Debt Ratio to 6.07 percent in fiscal year 2013-14 and 6.03 percent in fiscal year 2014-15. The actual General Fund Debt Ratio in future fiscal years will depend on a variety of factors, including actual debt issuance (which may include additional issuance approved in the future by the Legislature and, for general obligation bonds, the voters), actual interest rates, debt service structure, and actual General Fund revenues and transfers.

See the table “OUTSTANDING STATE DEBT, FISCAL YEARS 2008-09 THROUGH 2012-13” under “STATE DEBT TABLES” for certain historical ratios of debt service to General Fund receipts.

Economic Recovery Bonds

The California Economic Recovery Bond Act (“Proposition 57”) was approved by the voters on March 2, 2004. Proposition 57 authorized the issuance of up to \$15 billion in ERBs to finance the negative General Fund reserve balance as of June 30, 2004, and other General Fund obligations undertaken prior to June 30, 2004. Repayment of the ERBs is secured by a pledge of revenues from a one-quarter cent increase in the state’s sales and use tax (the “special sales tax”) that became effective July 1, 2004. In addition, as voter-approved general obligation bonds, the ERBs are secured by the state’s full faith and credit and payable from the General Fund in the event the dedicated sales and use tax revenue is insufficient to repay the bonds.

The entire authorized amount of ERBs was issued in three sales, in May and June 2004, and in February 2008. No further ERBs can be issued under Proposition 57, except for refunding bonds. The state issued refunding ERBs in 2009 to restructure the program in response to a drop in taxable sales caused by the recession, and in 2011 for debt service savings.

Three different sources of funds are required to be applied to the early retirement (generally by purchase or redemption) of ERBs: (i) all proceeds from the dedicated special sales tax in excess of the amounts needed, on a semi-annual basis, to pay debt service and other required costs of the bonds, (ii) all proceeds from the sale of specified surplus state property, and (iii) fifty percent of each annual deposit, up to \$5 billion in the aggregate, of deposits in the BSA (see “THE BUDGET PROCESS – Constraints on the Budget Process – Balanced Budget Amendment (Proposition 58)”). As of December 31, 2013, funds from these sources have been used for early retirement of approximately \$5.36 billion of bonds during fiscal years 2005-06 through 2012-13, including \$472 million which was transferred from the BSA in fiscal year 2006-07 and \$1.023 billion transferred from the BSA in fiscal year 2007-08.

The state accumulated approximately \$330 million in excess special sales tax and \$8 million from the sale of surplus state property up to January 1, 2014. The state will use these moneys to retire ERBs during the next six months.

The Governor suspended the BSA transfers in each of the fiscal years 2008-09 through 2013-14 due to the condition of the General Fund. The Governor has announced in the 2014-15 Governor’s Budget that the BSA transfer will be resumed in 2014-15, which will provide an estimated \$1.591 billion of additional funds for early retirement of ERBs. The Administration

currently estimates that by June 30, 2015 all of the ERBs will have been paid or provision for their payment will have been made through creation of escrow accounts.

Tobacco Settlement Revenue Bonds

In 1998 the state signed a settlement agreement (the “Master Settlement Agreement” or “MSA”) with the four major cigarette manufacturers (the “participating manufacturers” or “PMs”). Under the MSA, the PMs agreed to make payments to the state in perpetuity, which payments at the time were predicted to total approximately \$25 billion (subject to adjustments) over the first 25 years. Under a separate Memorandum of Understanding, half of the payments made by the cigarette manufacturers are paid to the state and half to certain local governments. The specific amount to be received by the state and such local governments is subject to adjustment under the MSA, including reduction of the PMs’ payments for decreases in cigarette shipment volumes by the PMs, payments owed to certain “Previously Settled States” and certain other types of offsets.

State law enacted in 2002 (the “Tobacco Securitization Law”) authorized the establishment of a special purpose trust to purchase the tobacco assets and to issue revenue bonds secured by the tobacco settlement revenues received beginning in the 2003-04 fiscal year. Legislation in 2003 amended the Tobacco Securitization Law to authorize a credit enhancement mechanism that requires the Governor to request an appropriation from the General Fund in the annual Budget Act to allocate funds from the General Fund for the payment of debt service and other related costs of the tobacco settlement revenue bonds secured by the second 2003 sale of tobacco settlement revenues in the event tobacco settlement revenues and certain other amounts are insufficient. The Legislature is not obligated to make any General Fund appropriation.

In 2003, two separate sales of these assets financed with revenue bonds (the “2003 Bonds”) produced about \$4.75 billion in proceeds which were transferred to the General Fund. In 2005 and 2007, the state refunded all of the original 2003 Bonds, generating additional proceeds of approximately \$1.783 billion, which were also transferred to the General Fund. This credit enhancement mechanism was applied to only the second 2003 sale of bonds and was continued when those bonds were refunded in 2005 and in 2013 (the “2005 Bonds” and the “2013 Bonds”). This credit enhancement mechanism only applies to the outstanding principal amount of approximately \$2.7 billion of 2005 and 2013 Bonds.

Tobacco settlement revenue bonds are neither general nor legal obligations of the state or any of its political subdivisions and neither the faith and credit nor the taxing power nor any other assets or revenues of the state or of any political subdivision is or shall be pledged to the payment of any such bonds; provided that, as described above, in connection with the issuance of the 2005 and 2013 Bonds, the state covenanted to request the Legislature for a General Fund appropriation in the event there are insufficient tobacco settlement revenues to pay debt service with respect to the 2005 and 2013 Bonds, and other available amounts, including the reserve funds with respect to the 2005 and 2013 Bonds, are depleted. Since the issuance of the 2005 Bonds, this appropriation has been requested and approved by the Legislature, to be utilized in the event tobacco settlement revenues and other available moneys are not sufficient to pay debt service. However, use of the appropriated moneys has never been required.

One of the reserve funds relating to the 2005 Bonds was used to make required debt service interest payments on the 2005 Bonds in 2011 and 2012 in part due to the withholding related to the declining tobacco consumption and disputes over declining PM market share. The total amount of the draws was approximately \$7.94 million. In April 2013 the reserve fund was replenished in full following the disbursements of the non-participating manufacturer settlement funds and receipt of the scheduled tobacco settlement revenues. As of January 1, 2014, the amount of the two reserve funds relating to the 2005 Bonds was \$253.3 million. If, in any future year tobacco settlement revenues are less than required debt service payments on the 2005 and 2013 Bonds in such year, additional draws on the reserve funds with respect to the 2005 and 2013 Bonds will be required. Future revenues in excess of debt service requirements, if any, will be used to replenish the reserve funds of the bonds. The state General Fund is not obligated to replenish the reserve funds, nor to request an appropriation to replenish the reserve funds.

Although the state cannot predict the amount of future tobacco settlement revenues, if the current trends continue, the amount of tobacco settlement revenues and other available moneys, including the reserve funds, may at some point in the future be insufficient to pay debt service on the 2005 and 2013 Bonds, and the Governor would be required to request an appropriation from the General Fund. However, the Legislature is not obligated to make an appropriation.

Cash Management Borrowings

As part of its cash management program, the state has regularly issued short-term obligations to meet cash management needs. See "CASH MANAGEMENT."

The following table shows the amount of RANs issued in the past five fiscal years and the current fiscal year.

TABLE 8
State of California Revenue Anticipation Notes Issued
Fiscal Years 2008-09 to 2013-14
(Dollars in Billions)

Fiscal Year	Type	Principal Amount	Date of Issue	Maturity or Redemption Date
2008-09	Notes Series A-1	\$1.2	October 23, 2008	May 20, 2009
	Notes Series A-2	3.8	October 23, 2008	June 22, 2009
	Notes Series B-1	0.5	March 23, 2009	June 23, 2009
2009-10	Interim Notes	1.5	August 27, 2009	September 29, 2009*
	Notes Series A-1	2.825	September 29, 2009	May 25, 2010
	Notes Series A-2	5.975	September 29, 2009	June 23, 2010
2010-11	Interim Notes	6.7	October 28, 2010	November 23, 2010*
	Notes Series A-1	2.25	November 23, 2010	May 25, 2011
	Notes Series A-2	7.75	November 23, 2010	June 28, 2011
2011-12	Interim Notes	5.4	July 28, 2011	September 22, 2011*
	Notes Series A-1	0.5	September 22, 2011	May 24, 2012
	Notes Series A-2	4.9	September 22, 2011	June 26, 2012
	Notes Series B	1.0	February 22, 2012	June 28, 2012
2012-13	Notes Series A-1	2.5	August 23, 2012	May 30, 2013
	Notes Series A-2	7.5	August 23, 2012	June 20, 2013
2013-14	Notes Series A-1	1.5	August 22, 2013	May 28, 2014
	Notes Series A-2	4.0	August 22, 2013	June 23, 2014

* Redemption date.

Source: State of California, Office of the State Treasurer

Indirect, Nonpublic or Contingent Obligations

Flood Litigation Judgment. In 2005, the state settled a lawsuit arising from liability for past flood damages through a stipulated judgment in the amount of \$428 million, which provided for the state to make annual payments of \$42.8 million, plus interest, for 10 years; the payments are subject to annual appropriation by the Legislature. The Legislature has included the required annual installment in each budget act since the settlement was approved. This matter is not treated as a “debt” of the state for any legal or constitutional purposes. The state understands that its annual installment payments have been pledged to secure certain debt instruments. The 2014-15 Governor’s Budget includes \$45 million for the required annual installment and concludes the fulfillment of the state’s obligation under the 2005 settlement.

Unemployment Insurance Fund Borrowing. As described in “STATE FINANCES – Unemployment Insurance,” commencing in fiscal year 2011-12, the state has been required to pay interest on loans made by the federal government to the state Unemployment Insurance (“UI”) Fund. The principal amount of these loans was about \$9.7 billion at the end of 2013, and is projected to be about \$8.8 billion at the end of 2014. The September 2013 interest payment of \$259 million was paid by the General Fund. The 2014-15 Governor’s Budget proposes \$231.6 million from the General Fund to make the 2014 interest payment.

Office of Statewide Health Planning and Development Guarantees. Pursuant to a law created in 1969, the Office of Statewide Health Planning and Development of the State of California (“OSHPD”) insures loans and bond issues for financing and refinancing of construction and renovation projects for nonprofit and publicly-owned healthcare facilities. This program (commonly called “Cal-Mortgage Loan Insurance”) is currently authorized by statute to insure up to \$3 billion for health facility projects.

State law established the Health Facility Construction Loan Insurance Fund (the “Fund”) as a trust fund which is continuously appropriated and may only be used for purposes of this program. The Fund is used as a depository of fees and insurance premiums and any recoveries and is the initial source of funds used to pay administrative costs of the program and shortfalls resulting from defaults by insured borrowers. If the Fund were unable to make payment on an insured loan or bond, state law provides for the State Treasurer to issue debentures to the holders of the defaulted loan or bond which are payable on parity with state general obligation bonds. All claims on insured loans to date have been paid from the Fund.

As of September 30, 2013, OSHPD insured 114 loans to nonprofit or publicly owned health facilities throughout California with an aggregate par amount of approximately \$1.686 billion. The cash balance of the Fund was approximately \$166.1 million as of September 30, 2013. OSHPD engaged Oliver Wyman Actuarial Consulting, Inc. to perform the biennial actuarial study of the Fund as of June 30, 2010, and the study was completed in August 2011 (the “2010 actuarial study”). Based upon a number of assumptions, the 2010 actuarial study concluded, among other things, that the Fund appeared to be sufficient, under the “expected scenario” to maintain a positive balance until at least fiscal year 2039-40. Even under the “most pessimistic scenario,” the 2010 actuarial study found that there was a 70 percent likelihood that the Fund’s reserves as of June 30, 2010 would protect against any General Fund losses until at least 2020-21, and a 90 percent likelihood that the Fund’s reserves as of June 30, 2010 would

protect against any General Fund losses until at least fiscal year 2016-17. An updated actuarial study for the period ended June 30, 2012 is in process. There can be no assurances that the financial condition of the Fund has not materially declined since the 2010 actuarial study. More information on the program can be obtained from OSHPD's website.

Equipment Lease/Purchase Program. The state Department of General Services operates a centralized program which allows state departments to acquire equipment, software or services under financing programs with approved vendors. The state departments make annual payments for the equipment from their support budgets, which are subject to annual appropriation by the Legislature. If for any reason the annual payments are not appropriated, the state department is obligated to return the equipment to the vendor. These contracts are represented as capital leases in the state's financial statements. As of January 1, 2014, the aggregate total of 59 contracts under this program was approximately \$126 million.

STATE FINANCES

The General Fund

The moneys of the state are segregated into the General Fund and over 1,000 other funds, including special, bond and trust funds. The General Fund consists of revenues received by the State Treasury and not required by law to be credited to any other fund, as well as earnings from the investment of state moneys not allocable to another fund. The General Fund is the principal operating fund for the majority of governmental activities and is the depository of most of the major revenue sources of the state. For additional financial data relating to the General Fund, see the financial statements incorporated in or attached to this APPENDIX A. See also "FINANCIAL STATEMENTS." The General Fund may be expended as a consequence of appropriation measures enacted by the Legislature and approved by the Governor (including the annual Budget Act), as well as appropriations pursuant to various constitutional authorizations and initiative statutes.

Budget Reserves

Special Fund for Economic Uncertainties

The SFEU is funded with General Fund revenues and was established to protect the state from unforeseen revenue reductions and/or unanticipated expenditure increases. The State Controller may transfer funds from the SFEU to the General Fund as necessary to meet cash needs of the General Fund and such transfers are characterized as "loans." The State Controller is required to return moneys so transferred without payment of interest as soon as there are sufficient moneys in the General Fund. At the end of each fiscal year, the State Controller is required to transfer from the SFEU to the General Fund any amount necessary to eliminate any deficit in the General Fund.

The legislation creating the SFEU (Government Code Section 16418) also contains a continuous appropriation authorizing the State Controller to transfer the unencumbered balance in the General Fund to the SFEU, as of the end of each fiscal year. However, if, at the end of any fiscal year in which it has been determined that there are revenues in excess of the amount that may be appropriated, as defined in subdivision (a) of Section 2 of Article XIII B of the state

Constitution, this transfer shall be reduced by the amount of the excess revenues. The estimates of the transfer shall be made jointly by the LAO and the Department of Finance. For a further description of Article XIII B, see “– State Appropriations Limit.” In certain circumstances, moneys in the SFEU may be used in connection with disaster relief.

For budgeting and accounting purposes, any appropriation made from the SFEU, other than appropriations contained in Government Code Section 16418, is deemed an appropriation from the General Fund. For year-end reporting purposes, the State Controller is required to add the balance in the SFEU to the balance in the General Fund so as to show the total moneys then available for General Fund purposes.

See Table 1 and footnote (i) in Table 4 for information concerning the recent balances in the SFEU and projections of the balances for the previous and current fiscal years. As in any year, the Budget Act and related trailer bills are not the only pieces of legislation which appropriate funds. Other factors, including re-estimates of revenues and expenditures, existing statutory requirements and additional legislation introduced and passed by the Legislature may impact the fiscal year-end balance in the SFEU.

Budget Stabilization Account

Proposition 58, approved in March 2004, created the BSA as a second budgetary reserve. Beginning with fiscal year 2006-07, a specified portion of estimated annual General Fund revenues (reaching a ceiling of 3 percent by fiscal year 2008-09) will be transferred by the State Controller into the BSA no later than September 30 of each fiscal year unless the transfer is suspended or reduced as described below. These transfers will continue until the balance in the BSA reaches \$8 billion or 5 percent of the estimated General Fund revenues for that fiscal year, whichever is greater. The annual transfer requirement will go back into effect whenever the balance falls below the \$8 billion or the 5 percent target. The annual transfers can be suspended or reduced for a fiscal year by an executive order issued by the Governor no later than June 1 of the preceding fiscal year. Proposition 58 also provides that one-half of the annual transfers shall be used to retire ERBs, until a total of \$5 billion has been used for that purpose. A total of \$1.495 billion of the \$5 billion amount has been applied to the retirement of ERBs. (See “STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Economic Recovery Bonds”).

Since 2007, each Budget Act has provided the Director of Finance the authority to transfer moneys from the BSA back into the General Fund in an amount determined by the Director of Finance to be sufficient to ensure there is a prudent General Fund balance. Using this authority, the Director of Finance ordered the transfer of the entire balance of \$1.495 billion from the BSA to the General Fund to address a fiscal emergency proclaimed by the Governor on January 10, 2008. Once moneys are transferred out of the BSA, pursuant to this authority, they will not be replenished by a future fiscal year’s annual transfer unless the Legislature, by statute, directs additional funds to be transferred from the General Fund into the BSA. Separate from the foregoing process for a budgetary transfer, the BSA may be used to make temporary cash flow loans to the General Fund, which must be repaid when the General Fund has available cash, as described under “– Inter-Fund Borrowings.”

Governor Brown suspended the General Fund transfer to the BSA in fiscal years 2011-12, 2012-13, and 2013-14. In addition, the previous Governor suspended the General Fund transfer to the BSA for fiscal years 2008-09 through 2010-11.

The 2014-15 Governor's Budget proposes a transfer of \$3.182 billion to the Budget Stabilization Account, half of which (\$1.591 billion) will be used to retire Economic Recovery Bonds, with the other half remaining in the BSA as a "rainy day" budgetary reserve.

In lieu of Proposition 58, and the Legislature's constitutional amendment proposal (Assembly Constitutional Amendment 4, Statutes of 2010, "ACA 4") scheduled to be on the November 2014 ballot, the 2014-15 Governor's Budget proposes a separate constitutional amendment to strengthen the "rainy day fund". The proposed constitutional amendment would (a) remove ACA 4 from the November 2014 ballot, (b) significantly amend (as described below) the existing rainy day fund requirements established by Proposition 58, and (c) create a more effective new reserve policy. In addition to a rainy day reserve for General Fund purposes, a new Proposition 98 reserve will be created to smooth out Proposition 98 programmatic spending. This new Proposition 98 reserve would not change the guaranteed level of funding dedicated to schools under Proposition 98. The amendment would be effective starting in fiscal year 2015-16.

The proposed policy would require these reserves to be funded by capital gains tax revenue spikes. The general purpose rainy day reserve would have a cap of 10 percent of General Fund tax revenues. In the event the Governor declares a fiscal emergency and the Legislature approves, the transfer could be suspended or reduced. The proposed amendment would authorize the state to redirect the rainy day fund transfer, or a portion thereof, to pay down specified debt obligations or to avoid issuing new debt. Transfers that would bring the balance in the reserve in excess of the 10-percent cap would be restricted for one-time costs or to pay down or avoid new debt.

Funds deposited in the Proposition 98 reserve count towards meeting Proposition 98 requirements in the fiscal year for which the transfer is made. The Proposition 98 reserve has a cap of 10 percent of total allocations to school districts and community college districts for that fiscal year. The Proposition 98 reserve may be appropriated to school districts and community college districts in any fiscal year in which Proposition 98 funding would be below the previous year Proposition 98 level adjusted for cost of living and population, as specified.

Inter-Fund Borrowings

Inter-fund borrowing is used to meet temporary imbalances of receipts and disbursements in the General Fund. In the event the General Fund is or will be exhausted, the State Controller is required to notify the Governor and the PMIB (comprised of the Director of Finance, the State Treasurer and the State Controller). The Governor may then order the State Controller to direct the transfer of all or any part of the moneys not needed in Special Funds to the General Fund, as determined by the PMIB. All money so transferred must be returned to the special fund from which it was transferred as soon as there is sufficient money in the General Fund to do so. Transfers cannot be made which will interfere with the objective for which such special fund was created, or from certain specific funds. In general, when moneys transferred to the General Fund in any fiscal year from any special fund pursuant to the inter-fund borrowing mechanism exceed

10 percent of the total additions to such special fund as shown in the statement of operations of the preceding fiscal year as set forth in the Budgetary/Legal Basis Annual Report of the State Controller, interest must be paid on such excess at a rate determined by the PMIB to be the current earning rate of the PMIA. This provision does not apply to temporary borrowings from the BSA or other accounts within the General Fund.

The amount of loans from the SFEU, the BSA and other internal sources to the General Fund, as of the end of any month is displayed in the most recent State Controller's Statement of General Fund Cash Receipts and Disbursements, on the first page under "Borrowable Resources – Outstanding Loans." See EXHIBIT 2 to APPENDIX A.

Any determination of whether a proposed borrowing from one of the special funds is permissible must be made with regard to the facts and circumstances existing at the time of the proposed borrowing. The Attorney General has identified certain criteria relevant to such a determination. For instance, amounts in the special funds eligible for inter-fund borrowings are legally available to be transferred to the General Fund if a reasonable estimate of expected General Fund revenues, based upon legislation already enacted, indicates that such transfers can be paid from the General Fund promptly if needed by the special funds or within a short period of time if not needed. In determining whether this requirement has been met, the Attorney General has stated that consideration may be given to the fact that General Fund revenues are projected to exceed expenditures entitled to a higher priority than payment of internal transfers, i.e., expenditures for the support of the public school system and public institutions of higher education.

Enactment of Proposition 22 on November 2, 2010 prohibited future interfund borrowing from certain transportation funds. However, legislation (Chapter 1, Statutes of 2012 – "SB 95") was enacted on February 3, 2012 to clarify the intent of Proposition 22, making those transportation funds available for short-term cash management borrowing purposes.

In addition to temporary inter-fund cash management borrowings described in this section, budgets enacted in the current and past fiscal years have included other budgetary transfers and long-term loans from Special Funds to the General Fund. In some cases, such budgetary loans and transfers have the effect of reducing internal borrowable resources.

The following table shows internal borrowable resources available for temporary cash management loans to the General Fund on June 30 of each of the fiscal years 2010-11 through 2013-14 and estimates the amount currently available based on the 2014-15 Governor's Budget. See EXHIBIT 1 and EXHIBIT 2 to APPENDIX A. The amount of internal borrowable resources fluctuates throughout the year.

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TABLE 9
Internal Borrowable Resources
(Cash Basis)

(Dollars in Millions)

	June 30					
	2010	2011	2012 ^(a)	2013	2014 ^(b)	2015 ^(b)
Available Internal Borrowable Resources	\$18,680.5	\$18,193.3	\$20,824.3	\$21,215.3	\$21,736.1	\$24,754.3
Outstanding Loans						
From Special Fund for Economic Uncertainties and Budget Stabilization Account	435.9	1,190.8	474.9	948.2	976.6	2,558.3
From Special Funds and Accounts	9,486.2	6,973.7	9,118.4	1,486.7	0	5,496.4
Total Outstanding Internal Loans	(9,922.1)	(8,164.5)	(9,593.3)	(2,434.9)	(976.6)	(8,054.7)
Unused Internal Borrowable Resources	\$8,758.4	\$10,028.8	\$11,231.0	\$18,780.4	\$20,768.6	\$16,699.6

^(a) Increase in internal borrowable resources at June 30, 2012 is largely a result of the SAIF program, which was in effect from September 2011 to April 2013. See “CASH MANAGEMENT – Cash Management Tools.”

^(b) Projected as of 2014-15 Governor’s Budget.

Source: Years ended June 30, 2010 through June 30, 2013: State of California, Office of the State Controller.
Years ending June 30, 2014 and 2015: State of California, Department of Finance.

State Warrants

No money may be drawn from the State Treasury except upon a warrant duly issued by the State Controller. The State Controller is obligated to draw every warrant on the fund out of which it is payable for the payment of money directed by state law to be paid out of the State Treasury; however, a warrant may not be drawn unless authorized by law and unless unexhausted specific appropriations provided by law are available to meet it. As described below, state law provides two methods for the State Controller to respond if the General Fund has insufficient “Unapplied Money” available to pay a warrant when it is drawn, referred to generally as “registered warrants” and “reimbursement warrants.” “Unapplied Money” consists of money in the General Fund for which outstanding warrants have not already been drawn and which would remain in the General Fund if all outstanding warrants previously drawn and then due were paid subject to the prior application of such money to obligations of the state with a higher priority. See “STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Cash Management Borrowings.” Unapplied Money may include moneys transferred to the General Fund from the SFEU and the BSA and internal borrowings from state Special Funds (to the extent permitted by law); however the state is not obligated to utilize interfund borrowings for the payment of state obligations if insufficient Unapplied Money is available for such payment. See “STATE FINANCES – Budget Reserves – Special Fund for Economic Uncertainties” and “Inter-Fund Borrowings.”

Registered Warrants

If a warrant is drawn on the General Fund for an amount in excess of the amount of Unapplied Money in the General Fund, after deducting from such Unapplied Money the amount, as estimated by the State Controller, required by law to be earmarked, reserved or set apart from the Unapplied Money for the payment of obligations having priority over obligations to which such warrant is applicable, the warrant must be registered on the reverse side as not paid because of the shortage of funds in the General Fund. The State Controller may issue registered warrants before exhausting all cash management techniques that could provide Unapplied Money to the General Fund. See “CASH MANAGEMENT.”

Registered warrants are interest bearing obligations that may be issued either with or without a maturity date. Most registered warrants bear interest at a rate designated by the PMIB up to a maximum of five percent per annum except, if the PMIB determines that it is in the best interests of the state to do so, the PMIB may fix the rate of interest paid on registered warrants at no more than 12 percent per annum. If issued with a maturity date, the principal and interest on such warrant will not be due until that date (although it may be optionally redeemed early if the state has sufficient unapplied money to do so) and the state may make other payments prior to that maturity date. If a registered warrant is issued without a maturity date, or its maturity date has occurred, it becomes redeemable by the holders on the date determined by the State Controller, with the approval of the PMIB.

State law generally requires that registered warrants be redeemable in the order they are issued but not prior to their maturity date, if any. The state issued approximately \$2.6 billion of registered warrants to pay certain obligations of the state not having payment priority under law commencing on July 2, 2009, all of which were called for early redemption on September 4, 2009. (The State Controller was able to manage cash resources to ensure that higher priority payments, such as for schools and debt service, were made on time in July and August 2009.) The issuance of the registered warrants permitted the state to pay Priority Payments with regular warrants which could be cashed.

Reimbursement Warrants

In lieu of issuing individual registered warrants to numerous creditors, state law provides an alternative procedure whereby the Governor, upon request of the State Controller, may authorize utilizing the General Cash Revolving Fund in the State Treasury to borrow from other state Special Funds to meet payments authorized by law. The State Controller may then issue “reimbursement warrants” (sometimes called “revenue anticipation warrants” or “RAWs”) for sale to investors to reimburse the General Cash Revolving Fund, thereby increasing cash resources for the General Fund to cover required payments. The General Cash Revolving Fund exists solely to facilitate the issuance of reimbursement warrants. Reimbursement warrants have a fixed maturity date which may not be later than the end of the fiscal year following the year in which they were issued.

The principal of and interest on reimbursement warrants must be paid by the State Treasurer on their respective maturity dates from any Unapplied Money in the General Fund and available for such payment. In the event that Unapplied Money is not available for payment on

the respective maturity dates of reimbursement warrants, and refunding warrants (see “– Refunding Warrants”) have not been sold at such times as necessary to pay such reimbursement warrants, such reimbursement warrants will be paid, together with all interest due thereon (including interest accrued at the original interest rate after the maturity date), at such times as the State Controller, with the approval of the PMIB, may determine.

The state has issued reimbursement warrants on several occasions in order to meet its cash needs when state revenues were reduced because of an economic recession, and the state incurred budget deficits. The state last issued reimbursement warrants in June 2002 and in June 2003.

Refunding Warrants

If it appears to the State Controller that, on the maturity date of any reimbursement warrant there will not be sufficient Unapplied Money in the General Fund to pay maturing reimbursement warrants, the State Controller is authorized under state law, with the written approval of the State Treasurer, to issue and sell refunding warrants to refund the prior, maturing reimbursement warrants. Proceeds of such refunding warrants must be used exclusively to repay the maturing warrants. In all other respects, refunding warrants are treated like reimbursement warrants, as described above.

Sources of Tax Revenue

The following is a summary of the state’s major tax revenues and tax laws. Further information on state revenues is contained under “PROPOSED FISCAL YEAR 2014-15 BUDGET,” and “STATE FINANCES – Recent Tax Receipts.” In fiscal year 2011-12, approximately 92 percent of the state’s General Fund revenues and transfers were derived from personal income taxes, corporation taxes, and sales and use taxes. See Table 16 titled “Comparative Yield of State Taxes – All Funds, Fiscal Years 2008-09 through 2013-14” for a summary of the actual and projected sources of the state’s tax revenue for those fiscal years.

Personal Income Tax

The California personal income tax is closely modeled after the federal income tax law. It is imposed on net taxable income (gross income less exclusions and deductions), with rates ranging from 1 percent to 12.3 percent. In addition, a 1 percent surcharge is imposed on taxable income above \$1 million and proceeds from such tax are dedicated to the Mental Health Services Fund. The personal income tax is adjusted annually by the change in the consumer price index to prevent taxpayers from being pushed into higher tax brackets without a real increase in income. Personal, dependent, and other credits are allowed against the gross tax liability. In addition, taxpayers may be subject to an alternative minimum tax (“AMT”), which is much like the federal AMT. The personal income tax structure is considered to be highly progressive. For example, the Franchise Tax Board indicates that the top 1 percent of taxpayers paid 41.1 percent of the total personal income tax in tax year 2011.

The 2014-15 Governor’s Budget revenue projections include the revenue expected from Proposition 30 (The Schools and Local Public Safety Protection Act of 2012) passed by the voters on November 6, 2012. This measure provides for an increase in the personal income tax

rate of one percent for joint filing taxpayers with income above \$500,000 and equal to or below \$600,000; two percent increase for incomes above \$600,000 and equal to or below \$1,000,000; and three percent increase for incomes above \$1,000,000. Tax rates for single filers will start at incomes one-half those for joint filers. These additional rates will remain in effect for seven years, commencing for calendar year 2012. The Administration estimates that the additional revenue from the addition of the three new tax brackets was \$3.4 billion in fiscal year 2011-12 and \$5.4 billion in fiscal year 2012-13, and will be \$5.6 billion in fiscal year 2013-14, and \$5.7 billion in 2014-15.

The 2014-15 Governor's Budget reflects assumptions regarding the behavioral impacts of federal tax law changes. The federal Economic Growth and Tax Relief Reconciliation Act of 2001 reduced taxes for dividend income, capital gains, and other income. These tax reductions were set to expire after 2010. However, late in 2010, they were extended through 2012. In addition, a 3.8 percent surtax on specified unearned income went into effect on January 1, 2013. For the 2014-15 Governor's Budget, the Department of Finance made assumptions that in 2012 some taxpayers would respond to the potential rate changes by accelerating approximately 20 percent of projected 2013 capital gains into 2012. It was also assumed that 4 percent of projected 2013 dividends and 1.1 percent of wages would be accelerated to 2012, thereby increasing receipts in fiscal year 2012-13, but reducing income tax receipts for fiscal year 2013-14. While federal tax cuts expired for high income earners (married filers over \$450,000) but were extended for other taxpayers, because Congress did not act until January 2013, it is expected that the income shifts that were assumed in the forecast actually occurred. See "RECENT DEVELOPMENTS – Recent Tax Receipts." There can be no assurance that acceleration of income into 2012 was not higher or lower than assumed, which could impact revenues in fiscal year 2013-14 negatively or positively.

TABLE 10
Personal Income Tax General Fund Revenues (PIT)
Fiscal Years 2008-09 through 2014-15

<u>Fiscal Year</u>	<u>Dollars In Millions</u>	<u>Percent Total General Fund Revenues And Transfers</u>
2008-09	\$43,376	52.4%
2009-10	44,852	51.5
2010-11	49,445	52.9
2011-12 ^(a)	54,261	62.5
2012-13 ^{(a)(e)}	65,332	65.4
2013-14 ^{(a)(e)}	64,287	64.2
2014-15 ^{(a)(e)}	69,764	66.8

^(a) Includes revenue from the higher rates imposed by Proposition 30 that are dedicated to the Education Protection Account. See "Proposition 98 and K-14 Funding."

^(e) Estimated.

Source: State of California, Department of Finance.

Taxes on capital gains realizations, which are linked to stock market and real estate performance, can add a significant dimension of volatility to personal income tax receipts. For example, capital gains tax receipts accounted for nearly 12 percent of General Fund revenues and

transfers in 1999-00 and 2000-01 but dropped below 4 percent in 2002-03 and 2009-10. The 2014-15 Governor's Budget projects that capital gains will account for 9.5 percent of General Fund revenues and transfers in fiscal year 2013-14 and 10 percent in fiscal year 2014-15.

The following table shows actual and projected tax revenues related to capital gains (which are included in the table showing total personal income tax receipts above):

TABLE 11
Revenues from Capital Gains
Fiscal Years 2008-09 through 2014-15

<u>Fiscal Year</u>	<u>Dollars In Millions</u>	<u>Percent Total General Fund Revenues And Transfers</u>
2008-09	3,863	5.5
2009-10	2,983	2.6
2010-11	4,526	5.0
2011-12	6,087	4.8
2012-13 ^(e)	10,082	10.1
2013-14 ^(e)	9,541	9.5
2014-15 ^(e)	10,488	10.0

^(e) Estimated.

Source: State of California, Franchise Tax Board provided calendar year actuals through 2011. From 2012 onward, State of California, Department of Finance estimated calendar year capital gains. Fiscal year totals shown in this table are estimated by adding 70 percent of calendar year total in first half of fiscal year to 30 percent of calendar year total in second half of fiscal year.

Sales and Use Tax

The sales tax is imposed upon retailers for the privilege of selling tangible personal property in California. Most retail sales and leases are subject to the tax. However, exemptions have been provided for certain essentials such as food for home consumption, prescription drugs, gas delivered through mains, and electricity. Other exemptions provide relief for a variety of sales ranging from custom computer software to aircraft.

The California use tax is imposed at the same rates as the regular sales tax on consumers of tangible personal property that is used, consumed, or stored in this state. Use tax applies to purchases from out-of-state vendors that are not required to collect tax on their sales. Use tax also applies to most leases of tangible personal property.

As of January 1, 2014, the breakdown for the uniform statewide state and local sales and use tax (referred to herein as the "sales tax") rate of 7.50 percent was as follows (many local jurisdictions have voted additional sales taxes for local purposes):

3.9375 percent imposed as a state General Fund tax;

0.25 percent dedicated to the Education Protection Account, per Proposition 30.

1.0625 percent dedicated to local governments for realignment purposes (Local Revenue Fund 2011);

0.5 percent dedicated to local governments for health and welfare program realignment (Local Revenue Fund);

0.5 percent dedicated to local governments for public safety services (Local Public Safety Fund);

1.0 percent local tax imposed under the Uniform Local Sales and Use Tax Law, with 0.25 percent dedicated to county transportation purposes and 0.75 percent for city and county general-purpose use; and

0.25 percent deposited into the Fiscal Recovery Fund to repay the state's ERBs (the "special sales tax").

Passage of Proposition 30 added a 0.25 percent additional sales tax rate from January 1, 2013 through December 31, 2016. Proposition 30 also constitutionally guarantees that the 1.0625 percent of the sales tax rate is dedicated to the cost of the realignment of certain defined public safety services programs from the state to the counties and explicitly states that this sales tax revenue does not constitute General Fund revenue for purposes of the Proposition 98 guarantee. The 1.0625 percent of the sales tax rate was expected to generate \$5.881 billion in fiscal year 2013-14 and \$6.311 billion in fiscal year 2014-15.

Legislation passed as part of the 2011 Budget Act imposes a use tax collection responsibility for certain out-of-state, and particularly internet, retailers who meet certain criteria. The new responsibility took effect in September 2012. In 2012-13, \$130 million in General Fund revenue was received as a result of this legislation. Additional General Fund revenue from this source is estimated at \$185 million in fiscal year 2013-14 and \$185 million in fiscal year 2014-15.

Existing law provides that 0.25 percent of the base state and local sales tax rate may be suspended in any calendar year upon certification by the Director of Finance, by November 1 in the prior year, that both of the following have occurred: (1) the General Fund reserve (excluding the revenues derived from the 0.25 percent special sales tax) is expected to exceed 3 percent of revenues in that fiscal year (excluding the revenues derived from the 0.25 percent special sales tax) and (2) actual revenues for the period May 1 through September 30 equal or exceed the previous May Revision forecast. The 0.25 percent rate will be reinstated the following year if the Director of Finance subsequently determines conditions (1) or (2) above are not met for that fiscal year. The Department of Finance estimates that the reserve level will be insufficient to trigger a reduction for calendar year 2014. See "Proposed Fiscal Year 2014-15 Budget – Summary of State Revenues and Expenditures" for a projection of the fiscal years 2013-14 and 2014-15 General Fund Reserve.

Existing law provides that the special sales tax will be collected until the first day of the calendar quarter at least 90 days after the Director of Finance certifies that all ERBs and related obligations have been paid or retired or provision for their repayment has been made or enough

sales taxes have been collected to pay all ERBs and related obligations to final maturity. At such time the special sales tax will terminate and the city and county portion of taxes under the uniform local sales and use tax will be automatically increased by 0.25 percent. The 2014-15 Governor's Budget anticipates that the ERBs will be repaid or funds to pay the outstanding ERBs will have been set aside in an irrevocable escrow fund by the end of fiscal year 2014-15. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Economic Recovery Bonds."

An appellate court decision from 2008 held that, from April 8, 1999 to June 30, 2008, two Dell entities and two providers of maintenance and warranty services had improperly collected from customers and remitted to the BOE use tax on optional service contracts that were sold with computers. A settlement was reached requiring the BOE to refund the tax with interest. About 191,000 claims totaling \$46 million (all funds) were received. These claims will likely be paid in fiscal year 2014-15.

The following table shows actual and projected sales and use tax revenue:

TABLE 12
Sales and Use Tax General Fund Revenues
Fiscal Years 2008-09 through 2014-15

<u>Fiscal Year</u>	<u>Dollars In Millions</u>	<u>Percent Total General Fund Revenues And Transfers</u>
2008-09	\$23,753	28.7%
2009-10	26,741	30.7
2010-11	26,983	28.9
2011-12	18,658	21.5
2012-13 ^(a)	20,482	20.5
2013-14 ^{(a)(e)}	22,920	22.9
2014-15 ^{(a)(e)}	24,071	23.0

^(a) Includes revenue from the higher rates imposed by Proposition 30 that are dedicated to the Education Protection Account.

^(e) Estimated.

Source: State of California, Department of Finance.

Corporation Tax

Corporation tax revenues are derived from the following taxes:

1. The Franchise Tax and the Corporate Income Tax are levied at an 8.84 percent rate on profits. The former is imposed on corporations for the privilege of doing business in California, while the latter is imposed on corporations that derive income from California sources but are not sufficiently present to be classified as doing business in the state.

2. Banks and other financial corporations are subject to the franchise tax plus an additional tax at the rate of 2 percent on their net income. This additional tax is in lieu of personal property taxes and business license taxes.

3. The AMT is similar to that in federal law. In general, the AMT is based on a higher level of net income computed by adding back certain tax preferences. This tax is imposed at a rate of 6.65 percent.

4. A minimum Franchise Tax of up to \$800 is imposed on corporations subject to the franchise tax but not on those subject to the corporate income tax. New corporations are exempted from the minimum franchise tax for the first year of incorporation.

5. Sub-Chapter S corporations are taxed at 1.5 percent of profits.

6. Fees paid by limited liability companies (“LLCs”), which account for 3.6 percent of corporation tax revenue, are considered “corporation taxes.”

Six actions have been filed contending that the Legislature’s modification of Revenue and Taxation Code Section 25128, which implemented the double-weighting of the sales factor in California’s apportionment of income formula for the taxation of multistate business entities, is invalid and/or unconstitutional. Now consolidated in one matter and collectively referred to as *Gillette Company v. Franchise Tax Board* (“*Gillette*”), the plaintiffs contend that the single-weighted sales factor specified in Section 25128 prior to amendment was contained within the Multistate Tax Compact (“MTC”) and therefore cannot be modified without repealing the legislation that enacted MTC. An adverse ruling in these cases would affect multiple taxpayers and create potential exposure to refund claims for past years of approximately \$750 million. The trial court ruled for the state in each of these matters, but the California Court of Appeal ruled on October 2, 2012 in favor of the taxpayers. The Franchise Tax Board has requested and the California Supreme Court has accepted review of this case. If the *Gillette* taxpayers are ultimately successful in their suit for refund, the vast majority of the revenue loss may not occur for several years. See “LITIGATION – Tax Cases.”

One significant revenue measure enacted as part of the 2012-13 Budget was repeal of the state’s participation in MTC, as a response to the *Gillette* litigation. By repealing its participation in MTC, the state will ensure that most taxpayers will not be allowed to use the equal weighted sales formula for apportioning income for calendar year 2012 and later tax years. Nonetheless, the current ruling in the *Gillette* case could result in a revenue loss of up to \$150 million in fiscal year 2012-13 (although these amounts could be recaptured if the state ultimately prevails in the case at the California Supreme Court).

Another portion of the legislation repealing the state’s participation in MTC finds and declares that there is a common law doctrine stating that elections affecting the computation of tax must be made on original tax returns. This provision seeks to render ineffective most attempts by taxpayers to file amended returns and obtain retroactive refunds, in the event that the state ultimately loses the *Gillette* cases. However, the implementation of this provision is likely to engender further litigation and the outcome cannot be assured.

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The following table shows actual and projected corporate income tax revenues:

TABLE 13
Corporate Income Tax Revenues
Fiscal Years 2008-09 through 2014-15

<u>Fiscal Year</u>	<u>Dollars In Millions</u>	<u>Percent Total General Fund Revenues And Transfers</u>
2008-09	\$9,536	11.5%
2009-10	9,115	10.5
2010-11	9,614	10.3
2011-12	7,233	8.3
2012-13 ^(e)	7,462	7.5
2013-14 ^(e)	7,971	8.0
2014-15 ^(e)	8,682	8.3

^(e) Estimated, see paragraph following Table 14.

Source: State of California, Department of Finance.

Legislation enacted in the budget acts of 2008, 2009, and 2010 is expected to significantly reduce corporation tax revenues. The third column of Table 14 shows that, while that legislation added over \$1 billion of revenue in fiscal years 2008-09 and 2009-10, by fiscal year 2011-12, that legislation is expected to generate, on a net basis, a revenue loss of almost \$1 billion. Starting in fiscal year 2012-13, that legislation is expected to generate revenue losses of about \$1.2 billion per year. However, the passage of Proposition 39 on November 6, 2012 reverses portions of these recent tax changes. Proposition 39 is expected to generate revenue gains of \$675 million in fiscal year 2013-14 and over \$726 million in fiscal year 2014-15 and subsequent years. The legislatively enacted law changes, together with Proposition 39, are expected to generate a net revenue loss of \$584 million in fiscal year 2013-14 and \$345 million in fiscal year 2014-15. Not all of the revenue generated by Proposition 39, however, benefits the General Fund, as the measure dedicates about half of the new revenues in fiscal years 2013-14 to 2017-18 to energy programs. See the table below for the impact of legislation *since 2008* and Proposition 39 on prior fiscal years. After the 2013-14 Budget, the Governor's new economic development program for the state was adopted by the Legislature. Key elements of this program included a new hiring credit, a sales tax exemption related to manufacturing and biotech research, and a new tax credit for businesses provided in exchange for investment and employment expansion in California. The new program will result in revenue gains of \$59 million in 2013-14, and \$189 million in 2014-15.

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TABLE 14
Impact of Legislation and Proposition 39 on Corporate Income Tax Revenues
Fiscal Years 2008-09 through 2014-15

(Dollars in Millions)

<u>Fiscal Year</u>	<u>Total</u>	<u>Impact of Enacted Legislation</u>	<u>Impact of Proposition 39</u>	<u>Net Impact of Law Changes Since 2008</u>
2008-09	9,536	\$1,093	\$0	\$1,093
2009-10	9,115	1,086	0	1,086
2010-11	9,614	54	0	54
2011-12	7,233	(890)	0	(890)
2012-13	7,462 ^(e)	(1,248)	320	(928)
2013-14	7,971 ^(e)	(1,259)	675	(584)
2014-15	8,682	(1,071)	726	(345)

^(e) Estimated.

Source: State of California, Department of Finance.

As shown in the table above, state tax law changes made several years ago traded short-term revenue gains for reduced corporate taxes in later years, which are now being seen. Even with this factor, the state Department of Finance has noted that corporation tax revenues have lagged significantly behind projections for the past year or more. The Department of Finance cannot determine at this time why revenue has lagged. There are several factors, however, that may be contributing to this result, including (i) greater growth in the use of tax credits than was anticipated, (ii) inaccurate estimates of the liability impact of the recent tax law changes, (iii) law changes that have led to changes to the pattern of cash receipts have made it more difficult for tax analysts to interpret cash flows, and (iv) the possible ability of corporations to take advantage of new tax reduction techniques. There is a significant lag (as much as two years) between the time weakness in tax revenues appears and the availability of the final, detailed tax return data on which analysis can be made to explain the results, so the Department of Finance is uncertain at this time with respect to the causes of this revenue weakness, and whether it will persist in the future.

Insurance Tax

The majority of insurance written in California is subject to a 2.35 percent gross premium tax. For insurers, this premium tax takes the place of all other state and local taxes except those on real property and motor vehicles. Exceptions to the 2.35 percent rate are certain pension and profit-sharing plans which are taxed at the lesser rate of 0.5 percent, surplus lines and non-admitted insurance at 3 percent and ocean marine insurers at 5 percent of underwriting profits.

The BOE ruled in December 2006 that the premium tax that insurers pay should be calculated on the basis of cash receipts rather than the value of premiums written as had been required by the Department of Insurance. This ruling is expected to result in a total loss of about \$400 million spread over several years, with the majority of the impact expected in fiscal year 2013-14 at \$223 million and fiscal year 2014-15 at \$149 million.

Other Taxes

Other General Fund taxes and licenses include: Cigarette Taxes; Alcoholic Beverage Taxes; Horse Racing License Fees; and Trailer Coach License Fees.

Special Fund Revenues

The state Constitution and statutes specify the uses of certain revenues. Such receipts are accounted for in various special funds. In general, special fund revenues comprise three categories of income:

Receipts from tax levies which are allocated to specified functions, such as motor vehicle taxes and fees and certain taxes on tobacco products.

Charges for certain services provided by the state government to individuals, businesses, or organizations, such as fees for the provision of business and professional licenses.

Rental royalties and other receipts designated for particular purposes (e.g., oil and gas royalties).

Motor vehicle-related taxes and fees are projected to account for approximately 26 percent of all special fund revenues in fiscal year 2014-15. Principal sources of this income are motor vehicle fuel taxes, registration and weight fees and vehicle license fees. In fiscal year 2014-15, \$11.8 billion is projected to come from the ownership or operation of motor vehicles. About \$4.4 billion of this revenue is projected to be returned to local governments. The remainder will be available for various state programs related to transportation and services to vehicle owners. For a discussion of Proposition 1A of 2004, which replaced a portion of vehicle license fees with increased property tax revenues, see “STATE FINANCES – Local Governments.”

Taxes on Tobacco Products

The state imposes an excise tax on cigarettes of 87 cents per pack and the equivalent rates on other tobacco products. Tobacco product excise tax revenues are earmarked as follows:

1. Fifty cents of the per-pack tax on cigarettes and the equivalent rate levied on non-cigarette tobacco products are deposited in the California Children and Families First Trust Fund and are allocated primarily for early childhood development programs.
2. Twenty-five cents of the per-pack tax on cigarettes and the equivalent rates levied on non-cigarette tobacco products are allocated to the Cigarette and Tobacco Products Surtax Fund. These funds are appropriated for anti-tobacco education and research, indigent health services, and environmental and recreation programs.
3. Ten cents of the per-pack tax is allocated to the state’s General Fund.

4. The remaining two cents of the per-pack tax is deposited into the Breast Cancer Fund.

Recent Tax Receipts

The following table shows the trend of major General Fund and total taxes per capita and per \$100 of personal income for the past five fiscal years and, the current fiscal year.

TABLE 15
Recent Tax Receipts

Fiscal Year	State Taxes Per Capita ^(a)		Taxes per \$100 of Personal Income	
	General Fund	Total	General Fund	Total
2008-09	\$2,153.11	\$2,579.07	\$4.97	\$5.95
2009-10	2,281.07	2,679.27	5.50	6.47
2010-11	2,409.84	2,866.28	5.69	6.77
2011-12 ^(b)	2,207.81	2,828.02	4.93	6.31
2012-13 ^{(b)(c)}	2,534.07	3,171.63	5.43	6.79
2013-14 ^{(b)(c)}	2,559.41	3,240.29	5.39	6.83
2014-15 ^{(b)(c)}	2,731.05	3,433.53	5.55	6.98

^(a) Data through fiscal year 2009-10 reflects population figures based on the 2010 Census. Data after fiscal year 2009-10 reflects July 1 population estimates benchmarked to the 2010 Census.

^(b) Includes revenues from Proposition 30.

^(c) Includes revenues from Proposition 39.

Source: State of California, Department of Finance.

The following table displays the actual and estimated revenues by major source for the past five fiscal years and the current fiscal year. This table shows taxes that provide revenue both to the General Fund and state special funds.

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TABLE 16
Comparative Yield of State Taxes – All Funds
Fiscal Years 2008-09 through 2014-15
(Modified Accrual Basis)
(Dollars in Thousands)

Fiscal Year	Sales and Use ^(a)	Personal Income ^(b)	Corporation ^(c)	Tobacco	Inheritance, Estate and Gift ^(d)	Insurance ^(e)	Alcoholic Beverage	Horse Racing	Motor Vehicle Fuel ^(f)	Motor Vehicle Fees ^(g)
2008-09	\$31,390,845	\$44,360,228	\$9,535,679	\$1,000,434	\$245	\$2,053,850	\$323,934	\$30,737	\$3,162,299	\$5,636,427
2009-10	33,527,230	45,625,240	9,114,589	922,965	252	2,238,872	311,242	12,740	3,149,143	6,786,009
2010-11	33,443,592	50,508,431	9,613,595	906,807	0	2,307,021	334,178	13,078	5,705,527	6,568,834
2011-12	31,245,211	54,635,590	7,962,603	897,355	0	2,415,781	346,241	15,838	5,544,530	5,908,046
2012-13 ^(h)	39,636,669	66,809,000	7,462,000	868,703	0	2,242,379	357,000	14,088	5,492,850	5,864,814
2013-14 ^(h)	44,214,991	65,662,000	7,971,000	838,518	0	2,143,000	350,000	14,684	6,014,023	6,052,182
2014-15 ^(h)	46,803,965	71,351,000	8,682,000	811,518	0	2,297,000	357,000	14,862	5,544,107	6,230,957

^(a) These figures:

- Fiscal years 2008-09 through 2011-12 include allocations to the General Fund, Public Transportation Account, State Fiscal Recovery Fund, Local Public Safety Fund, and the Local Revenue Fund (Realignment 1991). The figures do not include the Bradley Burns tax, dedicated to city and county operations.
- Fiscal years 2012-13 through 2014-15 include allocations to the General Fund, Public Transportation Account, State Fiscal Recovery Fund, Local Public Safety Fund, and both Local Revenue Funds (Realignment 1991 and 2011), and the Bradley Burns tax, which is dedicated to city and county operations.
- For fiscal years 2008-09 through 2010-11, includes the impact of a temporary increase in the General Fund sales and use tax rate from 5 percent to 6 percent, effective April 1, 2009 through June 30, 2011.
- Beginning in fiscal year 2010-11, includes the impact of the fuel tax swap that eliminated the General Fund portion of sales and use tax on motor vehicle gasoline fuel sales.
- Beginning in fiscal year 2011-12, includes the impact of the 2011 Realignment which redirects revenue attributable to a rate of 1.0625 percent to the Local Revenue Fund 2011.
- Beginning in fiscal year 2012-13, includes the impact of Proposition 30 (The Schools and Local Public Safety Protection Act of 2012). Proposition 30 temporarily increases the state sales tax by 0.25 percent effective January 1, 2013 through December 31, 2016. See "STATE FINANCES—Sources of Tax Revenue – Sales and Use Tax."
- Beginning in fiscal year 2013-14, includes revenue for a tax on Medi-Cal managed care premiums, with the rate being equal to the state General Fund sales tax rate.

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- (b) These figures include the revenue estimate for a 1.0 percent surcharge on taxpayers with taxable income over \$1 million, with the proceeds funding mental health programs pursuant to Proposition 63.
- Starting in fiscal year 2011-12, the figures also include the impact of Proposition 30. Proposition 30 temporarily adds three tax brackets for taxable incomes beginning at \$250,000 (\$500,000 joint) with rates of 10.3 percent, 11.3 percent, and 12.3 percent effective retroactive to January 1, 2012 through December 31, 2018.
- (c) These figures include impact of legislation on corporate tax revenues in the budget acts of 2008, 2009 and 2010, which accelerated corporate tax (CT) collections in fiscal years 2008-09 through 2010-11, and reduced CT collections starting in fiscal year 2011-12. See "STATE FINANCES – Sources of Tax Revenue – Corporation Tax" for a discussion of the impact of legislation on corporate income tax revenues.
- Starting in fiscal year 2012-13, these figures include the impact of Proposition 39, effective for tax years beginning January 1, 2013.
- Starting in fiscal year 2013-14, these figures include the impact of the economic development initiative, Chapters 69 and 70, Statutes of 2013 (AB 93 and SB 90)
- (d) From fiscal years 2008-09 through 2011-12, the state estate tax is based on the state death tax credit allowed against the federal estate tax. As a result, the federal Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) progressively reduced the state estate tax in calendar years 2002 through 2004 and eliminated it beginning in calendar year 2005. The EGTRRA was scheduled to sunset after 2010, at which time the federal estate tax would have been reinstated along with the state estate tax. The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, however, made changes to the estate tax for 2011 and 2012. One of those changes was an extension for 2011 and 2012 of the elimination of the state estate tax credit, which had been in effect since 2005.
- The American Taxpayer Relief Act of 2012 permanently eliminated state death tax credit (and thus the state portion of estate tax) beginning January 1, 2013.
- (e) Figures include insurance tax on Medi-Cal managed care plans from fiscal year 2008-09 through 2012-13. A Board of Equalization decision regarding the taxation of premiums on cash versus accrued basis has resulted in refunds of \$15 million in fiscal year 2008-09, \$0 million in fiscal year 2009-10, \$2 million in fiscal year 2010-11, about \$10 million in 2012-13, and estimated refunds of \$223 million and \$149 million in fiscal years 2013-14 and 2014-15, respectively.
- (f) These figures include motor vehicle fuel tax (gasoline), use fuel tax (diesel and other fuels), and jet fuel tax.
- Starting in fiscal year 2010-11, the figures include the revenue impact of the fuel tax swap that eliminated the General Fund portion of sales and use tax on motor vehicle gasoline fuel sales beginning in 2010-11.
- Excise Tax on Gasoline fuel: As part of the fuel tax swap implemented beginning July 1, 2010, the excise tax rate on gasoline fuel was increased from 18 cents to 35.3 cents in fiscal year 2010-11. It was set at 35.7 cents in fiscal year 2011-12, 36 cents in fiscal year 2012-13, and 39.5 cents in fiscal year 2013-14. This rate will be adjusted each year to maintain revenue neutrality with the elimination of the General Fund portion of sales tax on gasoline fuel.
- Excise Tax on Diesel fuel: Also as part of the fuel tax swap, the excise tax rate on diesel fuel was reduced from 18 cents to 13 cents in fiscal year 2011-12 and to 10 cents in fiscal year 2012-13 and 2013-14. This rate will also be adjusted each year to maintain revenue neutrality with a sales tax increase on diesel fuel.
- (g) Registration and weight fees, motor vehicle license fees and other fees. See "STATE FINANCES – Local Governments."
- Starting in fiscal year 2008-09 through fiscal year 2010-11, the figures include the impact of a temporary increase in the vehicle license fee from 0.65 percent to 1.15 percent, effective May 19, 2009 through June 30, 2011. Starting in fiscal year 2011-12, the vehicle license fee decreased from 1.15 percent to 0.65 percent.
- (h) Estimated for fiscal years 2012-13 to 2014-15.

Note: This table includes revenues accruing both to the General Fund and special funds. Some revenue sources are dedicated to local governments.

Source: Actual amounts for fiscal years 2008-09 through 2011-12: State of California, Office of the State Controller.

Estimated amounts for fiscal years 2012-13 through 2014-15: State of California, Department of Finance.

State Expenditures

The following table summarizes the major categories of state expenditures, including both General Fund and special fund programs for fiscal years 2007-08 through 2011-12.

TABLE 17
Governmental Cost Funds (Budgetary Basis)
Schedule of Expenditures by Function and Character
Fiscal Years 2007-08 to 2011-12

(Dollars in Thousands)

Function	Fiscal Year				
	2007-08	2008-09	2009-10 ^{(d)(e)}	2010-11 ^{(d)(e)(f)}	2011-12 ^(d)
Legislative, Judicial, Executive					
Legislative	\$ 338,482	\$ 330,594	\$ 323,371	\$ 325,244	\$ 331,052
Judicial	3,902,038	3,962,289	2,606,012	3,742,539	3,360,882
Executive	1,761,510	1,669,476	1,615,119	1,810,506	1,543,381
State and Consumer Services	1,272,910	1,248,522	1,079,608	1,173,185	1,249,034
Business, Transportation and Housing					
Business and Housing	245,062	228,408	215,295	227,899	239,838
Transportation ^(a)	10,058,388	7,331,284	7,178,962	7,109,753	5,452,535
Natural Resources	3,657,430	3,225,625	3,307,987	3,414,859	3,358,016
Environmental Protection	1,124,326	1,032,212	831,753	962,109	1,027,911
Health and Human Services	37,232,168	35,041,981	31,129,184	41,642,841	41,359,564
Correctional Programs	9,978,422	9,566,474	7,860,690	9,514,121	7,892,864
Education					
Education—K through 12	39,229,865	34,354,841	33,850,883	33,193,396	32,755,642
Higher Education	11,303,864	9,486,317	9,735,095	10,623,763	9,256,322
Labor and Workforce Development	421,116	414,307	374,059	370,993	700,449
General Government					
General Administration	1,796,460	1,728,781	1,711,273	1,757,991	1,712,184
Debt Service	4,988,637	5,693,895	6,049,251	6,222,307	6,561,871
Tax Relief	669,140	480,312	438,725	438,082	434,385
Shared Revenues	1,649,546	1,976,050	2,151,407	2,231,710	1,997,607
Other Statewide Expenditures	1,454,338	1,168,937	54,058	1,330,757	1,453,787
Expenditure Adjustment for Encumbrances ^(b)	(1,244,356)	551,826	1,785,703	18,316	2,195,656
Credits for Overhead Services by General Fund	(549,309)	(507,543)	(362,614)	(417,786)	(485,301)
Statewide Indirect Cost Recoveries	(88,045)	(94,458)	(80,454)	(100,543)	(109,807)
Total	<u>\$129,201,992</u>	<u>\$ 118,890,130</u>	<u>\$ 111,855,367</u>	<u>\$ 125,592,042</u>	<u>\$ 122,287,872</u>
Character					
State Operations	\$ 41,027,869	\$ 38,101,282	\$ 36,673,078	\$ 40,451,395	\$ 39,579,635
Local Assistance ^(c)	85,603,560	78,795,864	72,795,422	84,254,039	81,820,212
Capital Outlay	2,570,563	1,992,984	2,386,867	886,608	888,025
Total	<u>\$ 129,201,992</u>	<u>\$ 118,890,130</u>	<u>\$ 111,855,367</u>	<u>\$ 125,592,042</u>	<u>\$ 122,287,872</u>

^(a) For fiscal year 2007-08, the Transportation Investment Fund (Fund 3008) and the Transportation Deferred Investment Fund (Fund 3093) contracted for additional street and road repairs with monies provided by the General Fund per Revenue and Taxation Code Sections 7104 and 7107.

For fiscal year 2011-12, the Department of Transportation ("DOT") changed the basis of financial reporting from a modified accrual basis to a cash basis for the State Highway Account ("Fund 0042"), the Public Transportation Account ("Fund 0046"), the Traffic Congestion Relief Fund ("Fund 3007"), the Transportation Investment Fund ("Fund 3008"), and the Transportation Deferred Investment Fund ("Fund 3093"). This change resulted in a reduction of the reported expenditures by DOT in these funds for fiscal year 2011-12 due to expenditures incurred, but not paid in fiscal year 2011-12 not being accrued, and the fiscal year 2010-11 reported accruals being reversed. The change to cash basis financial reporting for these funds was done at the direction of the Department of Finance, in accordance with the following statutes: Streets and Highways Code Section 183(c), for Fund 0042; Public Utilities Code Section 99310.6, for Fund 0046; Government Code Section 14556.5(b), for Fund 3007; Revenue and Taxation Code Section 7104.3, for Fund 3008; and Revenue and Taxation Code Section 7105(g), for Fund 3093.

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- (b) For fiscal year 2008-09 Expenditure Adjustments for Encumbrances has an abnormal balance due to prior year reversal of over encumbered expenditures. Subsequent Budget adjustments per Executive Order S-09-08 issued July 31st did not allow for full expenditure of anticipated encumbered expenses. Health and Human Services, Corrections and Rehabilitation, and Higher Education had the most significant reductions. Fiscal years 2009-10 and 2010-11 have an abnormal balance due to the prior year reversal of over encumbered expenditures.
For fiscal year 2011-12, Expenditure Adjustments for Encumbrances has a large abnormal balance due to prior year reversal of over encumbered expenditures. The change to cash basis financial reporting the DOT in Funds 0042, 0046, 3007, 3008, and 3093 accounts for most of the abnormal balance.
- (c) In fiscal year 2009-10, Proposition 1A of 2004 was suspended when Governor Schwarzenegger declared a fiscal emergency allowing the state to offset local assistance expenditures with \$1.9 billion of property tax revenue borrowed from the local governments. The state repaid the obligation, plus interest, in June 2013. Additionally, \$1.7 billion of local property tax revenues were shifted to offset General Fund costs in fiscal year 2009-10, \$350 million were shifted in fiscal year 2010-11 and in fiscal year 2011-12 another \$43 million were shifted.
- (d) Executive Orders 10/11-A, 11/12-A and 12/13-A were issued by the Department of Finance, as authorized under Control Section 12.45 of the Budget Acts of 2009, 2010 and 2011, respectively, and pursuant to Government Code Sections 12472.5 and 13302, to defer the June 2010, June 2011 and June 2012 payroll expenditures for various governmental and nongovernmental cost funds to July 2010, July 2011 and July 2012. This affected all state departments paid through the uniform payroll system.
- (e) The Department of Conservation (“DOC”) did not submit the required year-end financial statements to the State Controller’s Office for fiscal years 2009-10 and 2010-11 in time to be included in the Budgetary/Legal Basis Annual Report (“BLBAR”). The DOC amounts reported in the BLBAR include the June 30, 2010 and June 30, 2011 cash balances, plus accruals, derived from actual activity reported through November 30, 2010 and December 5, 2011, respectively.
- (f) The State Air Resources Board (“ARB”) did not submit the required year-end statements for the Motor Vehicle Account in the State Transportation Fund, to the State Controller’s office for fiscal year 2010-11 in time to be included in the BLBAR. The Motor Vehicle Account amounts reported in the BLBAR include the ARB’s June 30, 2011 cash balances plus estimated (not reconciled) accrual amounts provided by ARB.

Source: State of California, Office of the State Controller.

State Appropriations Limit

The state is subject to an annual appropriations limit imposed by Article XIII B of the state Constitution (the “Appropriations Limit”). The Appropriations Limit does not restrict appropriations to pay debt service on voter-authorized bonds.

Article XIII B prohibits the state from spending “appropriations subject to limitation” in excess of the Appropriations Limit. “Appropriations subject to limitation,” with respect to the state, are authorizations to spend “proceeds of taxes,” which consist of tax revenues, and certain other funds, including proceeds from regulatory licenses, user charges or other fees to the extent that such proceeds exceed “the cost reasonably borne by that entity in providing the regulation, product or service,” but “proceeds of taxes” exclude most state subventions to local governments, tax refunds and some benefit payments such as unemployment insurance. No limit is imposed on appropriations of funds which are not “proceeds of taxes,” such as reasonable user charges or fees and certain other non-tax funds.

There are various types of appropriations excluded from the Appropriations Limit. For example, debt service costs of bonds existing or authorized by January 1, 1979, or subsequently authorized by the voters, appropriations required to comply with mandates of courts or the federal government, appropriations for qualified capital outlay projects, appropriations for tax refunds, appropriations of revenues derived from any increase in gasoline taxes and motor vehicle weight fees above January 1, 1990 levels, and appropriation of certain special taxes

imposed by initiative (e.g., cigarette and tobacco taxes) are all excluded. The Appropriations Limit may also be exceeded in cases of emergency.

The Appropriations Limit in each year is based on the Appropriations Limit for the prior year, adjusted annually for changes in state per capita personal income and changes in population, and adjusted, when applicable, for any transfer of financial responsibility of providing services to or from another unit of government or any transfer of the financial source for the provisions of services from tax proceeds to non-tax proceeds. The measurement of change in population is a blended average of statewide overall population growth, and change in attendance at local school and community college (“K-14”) districts. The Appropriations Limit is tested over consecutive two-year periods. Any excess of the aggregate “proceeds of taxes” received over such two-year period above the combined Appropriations Limits for those two years, is divided equally between transfers to K-14 districts and refunds to taxpayers.

The Legislature has enacted legislation to implement Article XIII B which defines certain terms used in Article XIII B and sets forth the methods for determining the Appropriations Limit. California Government Code Section 7912 requires an estimate of the Appropriations Limit to be included in the 2014-15 Governor’s Budget, and thereafter to be subject to the budget process and established in the Budget Act.

The following table shows the Appropriations Limit for fiscal years 2010-11 through 2014-15.

TABLE 18
State Appropriations Limit
(Dollars in Millions)

	Fiscal Year				
	2010-11	2011-12	2012-13	2013-14	2014-15
State Appropriations Limit	\$79,118	\$81,726	\$84,221	\$89,716	\$90,466 ^(a)
Appropriations Subject to Limit	-61,796	-61,952	-73,417 ^(a)	-75,079 ^(a)	-79,679 ^(a)
Amount (Over)/Under Limit	\$17,322	\$19,774	\$10,804 ^(a)	\$14,637 ^(a)	\$10,787 ^(a)

^(a) Estimated/projected.

Source: State of California, Department of Finance.

Proposition 98 and K-14 Funding

General. On November 8, 1988, the voters of the state approved Proposition 98, a combined initiative constitutional amendment and statute called the “Classroom Instructional Improvement and Accountability Act.” Proposition 98 changed state funding of public education below the university level and the operation of the Appropriations Limit, primarily by guaranteeing K-14 education a minimum level of funding (the “Proposition 98 minimum guarantee”). Proposition 98 (as modified by Proposition 111, enacted on June 5, 1990) guarantees K-14 education the greater of: (a) in general, a fixed percentage of General Fund revenues (“Test 1”), or (b) the amount appropriated to K-14 education in the prior year, adjusted for changes in state per capita personal income and enrollment (“Test 2”). A third test replaces

Test 2 in any year that the percentage growth in per capita General Fund revenues from the prior year plus one-half of one percent is less than the percentage growth in state per capita personal income (“Test 3”).

Legislation adopted prior to the end of the 1988-89 fiscal year implementing Proposition 98 determined the K-14 education’s funding guarantee under Test 1 to be 40.7 percent of General Fund tax revenues based on fiscal year 1986-87 appropriations. This percentage has since been adjusted to approximately 39.5 percent of fiscal year 1986-87 appropriations to account for subsequent changes in the allocation of local property taxes since these changes altered the share of General Fund revenues received by schools and other General Fund changes. The Proposition 98 guarantee has historically been calculated under Test 2, although Tests 1 and 3 have become more common in recent years. If Test 3 is used in any year, the difference between Test 3 and Test 2 becomes a “credit” (called the “maintenance factor”) to schools and is paid to them in future years when per capita General Fund revenue growth exceeds per capita personal income growth.

Proposition 98 permits the Legislature, by a two-thirds vote of both Houses (in a bill separate from the Budget Act) and with the Governor’s concurrence, to suspend the K-14 education’s minimum funding guarantee for a one-year period. The amount of the suspension is added to the maintenance factor, the repayment of which occurs according to a specified state constitutional formula, and eventually restores Proposition 98 funding to the level that would have been required in the absence of such a suspension. Suspending the minimum funding guarantee provides ongoing General Fund savings over multiple fiscal years until the Proposition 98 maintenance factor is fully repaid.

The Proposition 98 minimum guarantee has been funded historically from two sources: local property taxes and the General Fund. Any amount not funded by local property taxes is funded by the General Fund. Thus, local property tax collections represent an offset to General Fund costs in a Test 2 or Test 3 year. The passage of Proposition 30 has temporarily created a third source of funds. The newly created fund, the Education Protection Account (“EPA”), is available to offset Proposition 98 General Fund expenditures for fiscal years 2012-13 through 2018-19, freeing up General Fund resources for other purposes. See “Funding for Fiscal Years 2013-14 and 2014-15” below.

The process for calculating the Proposition 98 minimum guarantee involves recalculations for previous years based on revised estimates of state and local property taxes, average daily attendance (“ADA”), and civilian population. While some of these estimates are adjusted frequently, some may not be final for several years after the close of the fiscal year. Such changes in the estimates can result in significant adjustments to the guarantee, even if that year has ended. Therefore, additional appropriations may be required to fully satisfy the minimum guarantee for a prior year. These funds are referred to as “settle up” funds, and often include statutory language designating the fiscal year for which the funds count. The factors used to calculate Proposition 98 and how much settle-up is owed are considered final when certified as required by the state Education Code. Settle-up payments are made in future years at the discretion of the Legislature and the Governor.

Proposition 98 also contains provisions for the transfer of certain state tax revenues in excess of the Appropriations Limit to K-14 education in Test 1 years when additional moneys are available. No such transfer occurred for the 2012-13 and 2013-14 fiscal years, and no such transfer is anticipated for fiscal year 2014-15. See “STATE FINANCES – State Appropriations Limit.”

Funding for Fiscal Years 2013-14 and 2014-15. The 2014-15 Governor’s Budget continues to include the additional tax revenues generated by the passage of Proposition 30 in November, 2012. Proposition 30 requires that the resulting temporary increases in personal income tax and sales and use tax rates be deposited into the EPA. Appropriations from the EPA must be used to fund education expenditures and count towards meeting the Proposition 98 minimum guarantee. The funds deposited into the EPA offset \$7.2 billion in base Proposition 98 guarantee costs that would have otherwise been funded by the General Fund in fiscal year 2014-15. In addition, Proposition 39, the California Clean Energy Jobs Act, will provide \$726 million in revenue that is included in the calculation of the Proposition 98 minimum guarantee. Of this amount, \$355 million will be transferred to the Clean Energy Jobs Creation Fund in support of energy efficiency related activities in public schools and community colleges.

The 2014-15 Governor’s Budget Proposition 98 minimum guarantee level includes changes in revenues and “rebenching” of the guarantee (i.e., a change in the minimum guarantee percentage of General Fund revenues). Over the past few fiscal years, the major changes in revenues have been the inclusion of the revenues generated from the passage of Proposition 30 and Proposition 39, the ongoing increase in local tax revenues resulting from the elimination of redevelopment agencies, and the distribution of cash assets previously held by redevelopment agencies. In addition to these major changes, an overall increase in personal income tax, sales and use tax, and base local property tax revenues, result in an increase in the Proposition 98 minimum guarantee over the 2013 Budget Act levels. In fiscal year 2013-14, the Proposition 98 minimum guarantee is estimated to be \$56.8 billion, which is a \$1.5 billion increase over the 2013 Budget Act level. Proposition 98 funding in fiscal year 2014-15 is proposed to be \$61.6 billion, which is a \$6.3 billion increase over the 2013 Budget Act level. Of this amount, the General Fund share in fiscal year 2014-15 is \$45.1 billion, including \$7.2 billion in EPA revenues. In fiscal year 2014-15, it is estimated that the state will be in a Test 1 year.

The Proposition 98 minimum guarantee is also rebenched when the law requires an adjustment of the Test 1 percentage to reflect a shift in revenue or movement of programs into or out of the Proposition 98 minimum guarantee. In fiscal year 2013-14, the Proposition 98 minimum guarantee was rebenched to reflect the fund shift impact of a \$274 million increase (revised estimate) in offsetting local revenues as a result of the elimination of redevelopment agencies and the one-time distribution of cash assets held by redevelopment agencies. All rebenchings of the guarantee utilize a current value cost methodology, which results in a dollar for dollar change for each rebenching and provides a single and consistent methodology. Adjustments to the guarantee were made in fiscal year 2014-15 to reflect the one-time distribution of cash assets held by redevelopment agencies. The total impact of these rebenchings and the changes in revenues, in addition to other natural changes in Proposition 98 factors, result in the fiscal year 2014-15 Proposition 98 guarantee level of \$61.6 billion.

The 2014-15 Governor's Budget reflects General Fund Proposition 98 expenditures in fiscal years 2012-13 through 2014-15, as outlined in the table below.

TABLE 19
Proposition 98 Funding
(Dollars in Millions)

	2012-13		Fiscal Year 2013-14		2014-15	Change From Revised 2013-14 to Proposed 2014-15	
	Enacted^(a)	Revised^(c)	Enacted^(b)	Revised^(c)	Proposed^(c)	Amount	Percent
K-12 Proposition 98							
State General Fund	\$26,467	\$31,789	\$29,741	\$30,684	\$34,215	\$ 3,531	11.5%
Education Protection Account	6,922	6,509	5,572	6,263	6,451	188	3.0%
Local property tax revenue ^(d)	14,342	13,895	13,936	13,633	14,171	538	3.9%
Subtotals ^(e)	\$47,730	\$52,193	\$49,249	\$50,580	\$54,837	\$4,257	8.4%
CCC Proposition 98							
State General Fund	\$ 2,560	\$ 3,103	\$ 3,053	\$ 3,227	\$ 3,599	\$ 372	11.5%
Education Protection Account	855	805	689	774	797	23	3.0%
Local property tax revenue ^(d)	2,403	2,241	2,291	2,232	2,326	94	4.2%
Subtotals ^(e)	\$ 5,818	\$ 6,149	\$ 6,033	\$ 6,233	\$ 6,722	\$ 489	7.8%
Total Proposition 98							
State General Fund	\$29,027	\$34,893	\$32,794	\$33,911	\$37,814	\$ 3,903	11.5%
Education Protection Account	7,777	7,314	6,261	7,037	7,248	211	3.0%
Local property tax revenue ^(d)	16,745	16,135	16,226	15,866	16,497	631	4.0%
Totals^(e)	\$53,549	\$58,342	\$55,282	\$56,813	\$61,559	\$ 4,746	8.4%

(a) As of the 2012 Budget Act, June 27, 2012.

(b) As of the 2013 Budget Act, June 27, 2013.

(c) As of the 2014-15 Governor's Budget, January 9, 2014.

(d) Beginning in fiscal year 2011-12, local property tax revenues include amounts shifted to schools as a result of the elimination of redevelopment agencies; and fiscal years 2012-13, 2013-14, and 2014-15 include the one-time distribution of cash assets held by redevelopment agencies.

(e) Totals may not add due to rounding.

Source: State of California, Department of Finance.

Future Obligations. As explained above under "General," there are two forms of future obligations for the state General Fund which may be created under Proposition 98: maintenance factor and settle-up payments. Both of these obligations have been implemented in years leading up to fiscal year 2014-15. The following table shows the estimated Proposition 98 future obligations as of the 2014-15 Governor's Budget:

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TABLE 20
Proposition 98 Future Obligations Balances
(Dollars in Millions)

Year-End Balances:	Fiscal Year				
	2010-11 Estimated ^(a)	2011-12 Estimated ^(a)	2012-13 Estimated ^(a)	2013-14 Estimated ^(a)	2014-15 Estimated ^(a)
Maintenance Factor	\$10,314	\$10,606	\$5,530	\$7,910	\$4,549
QEIA Settle-up^(b)	1,531	410	410	410 ^(c)	0
Other Settle-Up	1,422	1,519	1,519	1,519 ^(c)	1,519

^(a) Proposition 98 factors and appropriations have been certified through fiscal year 2008-09.

^(b) The Quality Education Improvement Act ("QEIA") enacted the settlement of a lawsuit concerning the proper amount of the guarantee in fiscal years 2004-05 and 2005-06 that obligated the state to pay a total of \$2.7 billion in settle-up based on a statutory repayment plan. The final payment is proposed to be made in fiscal year 2014-15.

^(c) Included in "Underfunding of Proposition 98" in Table 7. See footnote (b) to Table 7.

Note: Proposition 98 budgetary deferrals, which are part of the "wall of debt," are not included in this Table. The 2014-15 Governor's Budget proposes to eliminate the balance of inter-year deferrals. A payment of \$2.5 billion is proposed in 2014-15 and additional payments of \$3.7 billion are proposed to be made toward deferral balances in 2012-13 and 2013-14. These payments would reduce deferrals from \$6.2 billion as of the 2013 Budget Act to \$2.5 billion in 2013-14 (the amount deferred from fiscal year 2013-14 to 2014-15) and eliminate the remaining deferral balance in 2014-15. See "DEFERRED OBLIGATIONS."

Maintenance factor payments are included in the multi-year projection (as shown in Table 3) developed by the Department of Finance based on factors known as of the 2014-15 Governor's Budget. The maintenance factor is adjusted by average daily attendance and per capita personal income growth each year. Therefore, even if a payment is made in a year, the outstanding balance can increase. Payments, as required by statute, are built into the multi-year projection as of the 2014-15 Governor's Budget totaling \$3.4 billion in fiscal year 2014-15, and \$1.2 billion in fiscal year 2015-16.

No maintenance factor payment is required in 2013-14 or 2016-17.

Local Governments

The primary units of local government in California are the 58 counties, which range in population from approximately 1,100 in Alpine County to approximately 9.9 million in Los Angeles County.

Constitutional and Statutory Limitations on Local Government

Counties are responsible for the provision of many basic services, including indigent health care, welfare, jails, and public safety in unincorporated areas. There are also 482 incorporated cities in California and thousands of special districts formed for education, utilities, and other services. The fiscal condition of local governments was changed when Proposition 13, which added Article XIII A to the state Constitution, was approved by California

voters in 1978. Proposition 13 reduced and limited the future growth of property taxes and limited the ability of local governments to impose “special taxes” (those devoted to a specific purpose) without two-thirds voter approval. Although Proposition 13 limited property tax growth rates, it also has had a smoothing effect on property tax revenues, ensuring greater stability in annual revenues than existed before Proposition 13 passed.

Proposition 218, another constitutional amendment enacted by initiative in 1996, further limited the ability of local governments to raise taxes, fees, and other exactions. (The limitations include requiring a majority vote approval for general local tax increases, prohibiting fees for services in excess of the cost of providing such service, and providing that no fee may be charged for fire, police, or any other service widely available to the public.)

In the aftermath of Proposition 13, the state provided aid to local governments from the General Fund to make up some of the loss of property tax moneys, including assuming principal responsibility for funding K-12 schools and community colleges. During the recession of the early 1990s, the Legislature reduced the post-Proposition 13 aid to local government entities other than K-12 schools and community colleges by requiring cities and counties to transfer some of their property tax revenues to school districts. However, the Legislature also provided additional funding sources, such as sales taxes, and reduced certain mandates for local services funded by cities and counties. See “STATE FINANCES – Sources of Tax Revenue – Sales and Use Tax” for a discussion of the impact of the Economic Recovery Bond issuances on local sales taxes.

The 2004 Budget Act, related legislation and the enactment of Proposition 1A in 2004 and Proposition 22 in 2010 (described below) dramatically changed the state-local fiscal relationship. These constitutional and statutory changes implemented an agreement negotiated between the Governor and local government officials (the “state-local agreement”) in connection with the 2004 Budget Act. One change relates to the reduction of the vehicle license fee (“VLF”) rate from 2 percent to 0.65 percent of the market value of the vehicle. In order to protect local governments, which had previously received all VLF revenues, the 1.35 percent reduction in VLF revenue to cities and counties from this rate change was backfilled (or offset) by an increase in the amount of property tax revenues they receive. This worked to the benefit of local governments because the backfill amount annually increases in proportion to the growth in property tax revenues, which has historically grown at a higher rate than VLF revenues, although property tax revenues declined between 2009-10 and 2011-12. This arrangement continues without change in the 2014-15 Governor’s Budget.

Pursuant to statutory changes made in conjunction with the 2009 Budget Act as initially enacted, the VLF rate increased from 0.65 percent to 1.15 percent effective May 19, 2009. Of this 0.50 percent increase, 0.35 percent flows to the General Fund, and 0.15 percent supports various law enforcement programs previously funded by the state General Fund. This increased VLF rate expired at the end of fiscal year 2010-11.

As part of the state-local agreement, voters at the November 2004 election approved Proposition 1A (“Proposition 1A of 2004”). Proposition 1A of 2004 amended the state Constitution to, among other things, reduce the Legislature’s authority over local government revenue sources by placing restrictions on the state’s access to local governments’ property,

sales, and VLF revenues as of November 3, 2004. A detailed description of the provisions of this constitutional amendment is set forth below under the caption “THE BUDGET PROCESS – Constraints on the Budget Process – Local Government Finance (Proposition 1A of 2004).”

The 2009 Budget Act (as amended by the revisions enacted on July 28, 2009) authorized the state to exercise its authority under Proposition 1A of 2004 to borrow an amount equal to about 8 percent of local property tax revenues, or \$1.9 billion, which was required to be repaid within three years. State law was also enacted to create a securitization mechanism for local governments to sell their right to receive the state’s payment obligations to a local government operated joint powers agency (“JPA”). This JPA sold bonds in a principal amount of \$1.895 billion in November 2009 to pay the participating local governments their full property tax allocations when they normally would receive such allocations. Pursuant to Proposition 1A of 2004, the state repaid the local government borrowing (which in turn repaid the bonds of the JPA) in June 2013, from the General Fund.

Proposition 22, adopted on November 2, 2010, supersedes Proposition 1A of 2004 and completely prohibits any future borrowing by the state from local government funds, and generally prohibits the Legislature from making changes in local government funding sources. Allocation of local transportation funds cannot be changed without an extensive process. The Proposition 1A borrowing done as part of the 2009 Budget Act (as amended by the revisions enacted on July 28, 2009) was not affected by Proposition 22.

Actions in recent budgets have sought to use moneys from redevelopment agencies (“RDAs”) to offset General Fund costs for Proposition 98. In a lawsuit relating to certain of these actions in fiscal years 2009-10 and 2010-11, which could have resulted in a General Fund liability of up to \$2.1 billion, the trial court denied the plaintiff’s petition and the appellate court affirmed the trial court ruling. This lawsuit is not impacted by the California Supreme Court ruling in the *Matosantos* case described below.

Redevelopment Agency Funds

The 2011 Budget Act included legislation (ABx1 27, Chapter 6, Statutes of 2011) seeking additional funds from RDAs as an alternative to the elimination of such agencies pursuant to the terms of related legislation (ABx1 26, Chapter 5, Statutes of 2011).

On December 29, 2011, in the case *California Redevelopment Association et al. v. Matosantos et al.*, the California Supreme Court upheld ABx1 26, which reaffirmed the state’s ability to eliminate RDAs, but also ruled that ABx1 27, which required RDAs to remit payments to schools in order to avoid elimination, was unconstitutional. In accordance with the Court’s order, RDAs were dissolved on February 1, 2012 pursuant to ABx1 26, and their functions have been taken over by successor agencies. (See “LITIGATION – Budget-Related Litigation – Actions Challenging Statutes Which Reformed California Redevelopment Law” for further information regarding the *Matosantos* case and other litigation on this subject.) Revenues that would have been directed to the RDAs are distributed to make “pass through” payments to local agencies that they would have received under prior law, and to successor agencies for retirement of the RDAs’ debts (also known as enforceable obligations) and for limited administrative costs.

The remaining revenues are distributed as property taxes to cities, counties, school and community college districts, and special districts under existing law.

Accurately estimating the property tax revenue available for the affected taxing entities after the payment of enforceable obligations was initially a challenge. This is because comprehensive information concerning the amount of property tax expended by the former RDAs for purposes that qualify as enforceable obligations was not available prior to the enactment of ABx1 26. Now that information from five payment cycles is available, the Department of Finance can provide better estimates of future Proposition 98 General Fund savings stemming from the RDA dissolution process.

The 2013 Budget Act anticipated \$2.1 billion Proposition 98 General Fund savings resulting from the dissolution of RDAs in 2012-13, which is the same amount that was estimated at the 2014-15 Governor's Budget. For the 2014-15 Governor's Budget, Proposition 98 General Fund savings are anticipated to be \$1.1 billion in fiscal year 2013-14, which is \$400 million below the amount estimated at the 2013 Budget Act. Projected Proposition 98 General Fund savings in 2014-15 are \$785 million, which is \$134 million below the amount projected at the 2013 Budget Act. On an ongoing basis, Proposition 98 General Fund savings are anticipated to be at least \$1 billion per year beginning in 2016-17, with annual growth proportionate to the changes in property tax growth, and the rate at which the enforceable obligations of the former RDAs are retired.

The decline in the projected amount of property tax received by schools in fiscal years 2013-14 and 2014-15 is primarily due to three factors. These are (1) the future unavailability of RDA cash reserves that were used instead of property tax to pay prior enforceable obligations, (2) the ability of cities and counties that have received a Finding of Completion to create enforceable obligations for the repayment of loans provided to their RDAs prior to the dissolution, and (3) court rulings that inhibit the state's ability to compel cities and counties that illegally shifted property tax revenues from their RDAs before the dissolution to remit those revenues to the affected taxing entities. As the debts of the former RDAs are gradually retired, however, the amount of property tax received by K-14 schools and the other affected taxing entities should show modest annual growth notwithstanding these factors.

Local governments have disputed the implementation of AB 1484 and litigation is pending and expected to be filed in the future on this subject.

Property Tax Revenues

Although the property tax is a local revenue source, the amount of property tax generated each year has a substantial impact on the state budget because local property tax revenues allocated to K-14 schools typically offset General Fund expenditures. Assessed value growth is estimated based on twice yearly surveys of county assessors and evaluation of real estate trends.

Assessed value growth is estimated based on statistical modeling and evaluations of real estate trends. The median sales price of new and existing homes rose by over 12 percent in 2012 and 24 percent in 2013 (with activity in the 2013 calendar year driving fiscal year 2014-15 assessed valuations for property tax purposes). While sales volumes declined by approximately

3 percent in 2013, the impact on 2014-15 property tax revenues will be moderated by the significant increase in 2013 median prices, coupled with the reassessment to current market value of homes whose assessed values were significantly reduced during the market downturn. This increase in property valuations, coupled with continuing declines in the number of foreclosures, indicates the state's real estate market is in a period of rebound. Despite this overall increase, however, there are still areas where sales volumes and property values continue to stagnate.

Statewide property tax revenues are estimated to increase 4.2 percent in fiscal year 2013-14 and 6.3 percent in fiscal year 2014-15. See Table 19 (Proposition 98 Funding) for information on the impact of these growth rates on the funding of the Proposition 98 guarantee. Property tax estimates used in the calculation of the guarantee are based on growth in statewide property taxes, but also include other factors such as excess tax, redevelopment agency payments, and Educational Revenue Augmentation Fund transfers.

Realigning Services to Local Governments

The 2011 Budget Act included a major realignment of public safety programs from the state to local governments ("AB 109"). The realignment was designed to move program and fiscal responsibility to the level of government that can best provide the service, eliminate duplication of effort, generate savings, and increase flexibility. The implementation of the Community Corrections Grant Program authorized by AB 109 moved lower-level offenders from state prisons to county supervision and reduced the number of parole violators in the state's prisons. Other realigned programs include local public safety programs, mental health, substance abuse, foster care, child welfare services, and adult protective services. The 2011 Realignment is funded through two sources: (1) a state special fund sales tax of 1.0625 percent (totaling \$5.8 billion in fiscal year 2013-14) and (2) \$467.3 million in vehicle license fees (for fiscal year 2013-14). As a result of the realignment, the state expects General Fund savings from the realigned programs to be about \$2.5 billion annually beginning in fiscal year 2011-12. In fiscal year 2011-12, about \$2.1 billion of these savings was achieved from a reduction in the Proposition 98 Guarantee, and that figure is currently estimated to grow to \$2.2 billion in fiscal year 2012-13 and \$2.5 billion in fiscal year 2013-14. A lawsuit was filed challenging this calculation of the Proposition 98 Guarantee and on June 1, 2012, the trial court ruled in favor of the state and denied the petition for writ of mandate for recalculation of the Guarantee; however, plaintiffs have appealed this decision. See "LITIGATION – Budget Related Litigation – Actions Challenging School Financing."

Economic Development and Job Creation

Chapter 69, Statutes of 2013 (AB 93) repealed provisions in current law related to economic development areas and created in its place a new program of job creation and economic development incentives. AB 93 was further amended by Chapter 70, Statutes of 2013 (SB 90). Currently, the state has two types of Economic Development Areas: Enterprise Zones and Local Agency Military Base Recovery Areas. Special tax incentives in the form of hiring credits, sales and use tax credits, business expense deductions, net operating loss deductions, net interest deductions, and employee wage credits are available to individuals and businesses that

operate a business or invest in a business located within certain economically depressed areas in the state.

AB 93 ceases operation of the current economic development areas as of January 1, 2014. The sales tax credit provisions under the current program will be repealed effective January 1, 2014, and the hiring credit provisions will be repealed effective January 1, 2019. The hiring credit would continue to apply for qualified employees hired within the 60-month period prior to January 1, 2014, and the qualified wages paid would continue to qualify for the credit after January 1, 2014. Leftover credits from the current program may be carried forward to the succeeding 10 taxable years, if necessary.

AB 93 and SB 90 create a new program of job creation and economic development incentives by instituting a development program which includes the following elements:

A sales exemption from the state portion of the sales and use tax on purchases of qualified tangible property for certain businesses primarily engaged in manufacturing, research and development;

A hiring credit for qualifying full-time employees for businesses in certain designated census tract areas; and

An incentive fund to provide a tax credit to certain businesses in exchange for investment and employment expansion in California.

Based on current projections, the provisions in AB 93 and SB 90 are expected to be revenue neutral over the next five fiscal years. In the long run, assuming the sunset dates for the new programs are not extended, substantial revenue increases would be expected.

Trial Courts

Prior to legislation enacted in 1997, local governments provided the majority of funding for the state's trial court system. The legislation consolidated the trial court funding at the state level in order to streamline the operation of the courts, provide a dedicated revenue source, and relieve fiscal pressure on the counties. In addition, legislation enacted in 2008 provides California's court system with increased fees and fines to expand and repair its infrastructure to address significant caseload increases and reduce delays. The fees raised by this legislation were intended to support debt service on lease revenue bonds and other appropriate evidences of indebtedness used to pay qualified infrastructure costs in an amount of up to \$5 billion. The SPWB has issued \$1.2 billion in lease revenue bonds to date to finance such costs. Additional legislative authorization is required prior to the issuance of any additional lease-revenue bonds for court construction. The 2014-15 Governor's Budget includes an appropriation of \$54.2 million to pay an annual service fee to the private developer of the new Long Beach Courthouse. Service fees for the Long Beach Courthouse, which are subject to annual appropriation by the Legislature, are expected to be approximately \$2 billion over a period of 35 years.

The state's trial court system will receive approximately \$1.9 billion in state resources in fiscal year 2013-14 and \$2 billion in fiscal year 2014-15, as well as \$499 million in resources from counties in each fiscal year. The 2013 Budget Act included a General Fund augmentation of \$60 million to support the state's trial court system and the 2014-15 Governor's Budget includes an additional \$100 million in ongoing General Fund resources. The 2014-15 Governor's Budget also includes \$123.6 million for 15 court construction projects, including \$101.7 million from lease revenue bonds, with debt service expected to be paid from future court construction revenues.

Welfare System

Under the CalWORKs (as such term is defined herein) program, counties are given flexibility to develop their own plans, consistent with state law, to implement the program and to administer many of its elements. Counties are required to provide "general assistance" aid to certain persons who cannot obtain welfare from other programs.

Health and Human Services

CalWORKs

The state provides welfare benefits to certain adults and children living in the state. Although some of these benefits are available to legal noncitizens, the majority of these benefits are available only to citizens.

These benefits generally take the form of cash payments to beneficiaries, or programs pursuant to which beneficiaries receive food or assistance in procuring employment. Many of these programs are administered by counties within the state, and paid with a combination of federal, state and local funds. Counties are given flexibility to develop their own plans, consistent with state law, to implement the program and to administer many of its elements.

The federal government pays a substantial portion of welfare benefit costs, subject to a requirement that states provide significant matching funds. Federal law imposes detailed eligibility and programmatic requirements in order for states to be entitled to receive federal funds. Federal law also imposes time limits on program availability for individuals, and establishes certain work requirements. The primary federal law establishing funding and eligibility, and programmatic requirements is The Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (P.L. 104-193, the "Law"). Significant elements of the Law include: (i) Temporary Assistance for Needy Families ("TANF"), a block grant program; and (ii) the Supplemental Nutrition Assistance Program at the federal level (referred to as "CalFresh" in California, and formerly known as "food stamps").

Chapter 270, Statutes of 1997, embodies California's response to the federal welfare systems, called California Work Opportunity and Responsibility to Kids ("CalWORKs"). Consistent with the federal law, CalWORKs contains time limits on the receipt of welfare aid. The centerpiece of CalWORKs is the linkage of eligibility to work participation requirements.

Caseload under CalWORKs is projected to decrease in fiscal year 2014-15 as compared to revised fiscal year 2013-14 levels. CalWORKs caseload projections are 545,647 cases in

fiscal year 2013-14 and 529,367 cases in fiscal year 2014-15. The fiscal year 2014-15 projected caseload represents a major decline from the early 1990s, when caseload peaked at 921,000 cases in fiscal year 1994-95. CalWORKs became effective on January 1, 1998. At the federal and state levels, TANF and CalWORKs, respectively, replaced the former Aid to Families with Dependent Children program. CalWORKs caseload from 1998 through fiscal year 2014-15 is estimated to have declined by approximately 17.4 percent.

The state's required expenditures in connection with the Law are referred to as "Maintenance of Effort" or "MOE." California's required MOE is generally equal to 75 percent of federal fiscal year ("FFY") 1994 historic expenditures. However, in order to qualify for that level of MOE, the state is required to demonstrate a 50 percent work participation rate among all families. The federal government determined that the state failed to meet this requirement for FFYs 2007 through 2010, and the state is therefore subject to a penalty. The federal government waived the penalty for FFY 2007, but required the state to increase the required MOE to 80 percent of FFY 1994 historic expenditures. As a result, the state was required to increase its MOE expenditure by approximately \$180 million. The 2014-15 Governor's Budget continues to reflect this increase in MOE spending. Currently, the state is seeking relief from the FFYs 2008, 2009, and 2010 penalties. If the state is unsuccessful, and the state is unable to provide an acceptable corrective compliance plan, penalties (currently estimated to be approximately \$47.7 million, \$113.6 million, and \$179.7 million for FFYs 2008, 2009, and 2010, respectively) may be imposed, which would be payable in future fiscal years. Any penalties from failing to meet federal work participation requirements would be in addition to the approximately \$180 million increased MOE requirement.

In fiscal year 2013-14, \$541.7 million in federal TANF will be transferred to the California Student Aid Commission to offset General Fund costs in Cal Grants. For fiscal year 2014-15, \$544.9 million in federal TANF will be transferred to the California Student Aid Commission for this purpose.

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The following table shows CalWORKs caseload and General Fund expenditures for state fiscal years 2009-10 through 2014-15.

TABLE 21
CalWORKs Expenditures

(Dollars in Billions)

<u>Fiscal Year</u>	<u>Caseload</u>	<u>General Fund Expenditures</u>
2009-10	553,347	2.032
2010-11	586,659	2.240
2011-12 ^(a)	575,988	1.158
2012-13	559,920	1.545
2013-14 ^{(b) (c)}	545,647	1.207
2014-15 ^{(b) (d)}	529,367	0.641

^(a) Beginning in FY 2011-12, CalWORKs General Fund expenditures reflect a \$1.1 billion ongoing annual savings as a result of redirecting 1991-92 realignment revenues from mental health to fund CalWORKs grants, pursuant to Chapter 13, Statutes of 2011.

^(b) Estimated.

^(c) Reflects an anticipated \$300 million General Fund savings through redirecting a portion of 1991-92 realignment revenues from indigent health to CalWORKs, pursuant to Chapter 24, Statutes of 2013.

^(d) Reflects \$900 million General Fund savings from redirecting a portion of 1991-92 realignment revenue from indigent health to CalWORKs.

Chapter 47, Statutes of 2012 (SB 1041) made significant changes to the CalWORKs programs as follows:

Created a prospective 24-month time limit on cash assistance and employment services for adults. After two years, adults must meet federal work participation requirements to remain eligible for cash aid for up to 24 additional months.

Provided counties some flexibility by allowing up to 20 percent of the adults to extend their time beyond 24 months to complete their educational goals or find a job.

Provided up to two years for clients to transition to the new program and be provided the skills necessary to find employment as the economy continues to recover.

To maximize successful outcomes under the new program structure, the 2013-14 budget included: (1) an increase of \$142.8 million for counties to enhance and expand the array of employment services and job development activities available to program participants, and (2) partial year funding of \$47 million General Fund (\$138 million General Fund annually) to

implement additional proven appraisal protocols, promote family stabilization and barrier removal, and provide enhanced subsidized employment opportunities.

Chapter 24, Statutes of 2013 (AB 85), increases CalWORKs grants levels by 5 percent, effective March 1, 2014, to be funded with 1991-92 realignment sales tax revenue growth funds. The grant increase is estimated to cost \$57.5 million in 2013-14 and \$168 million annually thereafter. Based on current revenue projections, the estimated 2014-15 costs of the grant increase will exceed available realignment revenues by \$6.3 million. The 2014-15 Governor's Budget includes \$6.3 million General Fund to cover this projected shortfall to fully fund the grant increase, as required by AB 85. Future grant increases are subject to projections of realignment sales tax growth revenues available after the ongoing cumulative costs of all prior grant increase are fully funded.

SSI/SSP

The federal Supplemental Security Income ("SSI") program provides a monthly cash benefit to eligible seniors and persons with disabilities who meet the program's income and resource requirements. In California, the SSI payment is augmented with a State Supplementary Payment ("SSP") grant. The 2014-15 Governor's Budget includes approximately \$2.8 billion for the SSI/SSP program from the General Fund for fiscal year 2014-15, 1.2 percent more than the revised fiscal year 2013-14 funding level. The average monthly caseload in this program is estimated to be 1.3 million recipients in fiscal year 2014-15, a 0.8 percent increase over the revised fiscal year 2013-14 projected level.

Health Programs

Medi-Cal – Medi-Cal, California's Medicaid program is a health care entitlement program for low-income individuals and families who receive public assistance or otherwise lack health care coverage. Medi-Cal serves approximately one in five Californians. Federal law requires Medi-Cal to provide basic services such as doctor visits, laboratory tests, x-rays, hospital inpatient and outpatient care, hospice, skilled nursing care, and early periodic screening, diagnosis and treatment. Also, federal matching funds are available if states choose to provide any of numerous optional benefits. California's Federal Medical Assistance Percentage is 50 percent, which is the share of federal funding for standard program benefits. There are also federal funds in the Medi-Cal budget for a number of Medi-Cal programs or supplemental payments that are matched with local funds that do not appear in state funding totals or that receive a higher matching rate. A wide range of public and private providers and facilities delivers these services. Providers are reimbursed by the traditional fee-for-service method or by managed care plans that receive capitated payments from the state. Approximately 6.3 million Medi-Cal beneficiaries (more than half of the people receiving Medi-Cal benefits and services) are currently enrolled in managed care plans.

Average monthly caseload in Medi-Cal is projected to be 9.2 million in fiscal year 2013-14. Caseload is expected to increase in fiscal year 2014-15 by approximately 0.9 million, or 10.2 percent, to 10.1 million people. This increase is largely due to the implementation of federal health care reform and the shift of children from the Healthy Families program to Medi-Cal. Caseload would increase by 1 percent absent these changes.

The following table shows Medi-Cal expenditures for the fiscal years 2010-2011 through 2013-14 and the proposed amounts for fiscal year 2014-15.

TABLE 22
Medi-Cal Expenditures

(Dollars in Billions)

<u>Fiscal Year</u>	<u>General Fund</u>	<u>Other State Funds</u>	<u>Federal Funds</u>	<u>Total^(a)</u>
2010-11	\$12.5	\$8.9	\$30.7	\$52.1
2011-12	15.2	2.1	26.4	43.7
2012-13	14.9	6.4	28.3	49.5
2013-14 ^(b)	16.2	9.8	43.6	69.7
2014-15 ^(c)	16.9	10.9	45.8	73.5

^(a) Totals may not add due to rounding.

^(b) Estimated.

^(c) Proposed.

The 2014-15 Governor’s Budget includes the following major General Fund elements:

Net Savings of \$149.6 million in fiscal year 2013-14 and \$159.4 million in fiscal year 2014-15 due to the implementation of the Coordinated Care Initiative. Chapter 33, Statutes of 2012 (SB 1008) and Chapter 45, Statutes of 2012 (SB 1036) authorized the Coordinated Care Initiative in which persons eligible for both Medicare and Medi-Cal (dual eligibles) will receive medical, behavioral health, long-term supports and services, and home and community-based services coordinated through a single health plan.

Net costs of \$124 million in fiscal year 2013-14 and \$250.8 million in fiscal year 2014-15 to pay for the federally required and optional expansion of coverage under federal health care reform. See “Health Care Reform.”

Costs of \$231.8 million in fiscal year 2014-15 for rate increases to Medi-Cal managed care health plans.

Litigation is pending with respect to certain cost reductions implemented by the state. See “LITIGATION – Actions Regarding Medi-Cal Reimbursements and Fees.”

Health Care Reform – The federal Affordable Care Act (“ACA”) increases access to public and private health care coverage through various programmatic, regulatory, and tax incentive mechanisms. To expand coverage, the ACA provides for: (1) the health insurance exchange, a new marketplace in which individuals who do not have access to public coverage or affordable employer coverage can purchase insurance and access federal tax credits, and (2) two expansions of Medicaid – a mandatory expansion by simplifying rules affecting eligibility,

enrollment, and retention; and an optional expansion to adults with incomes up to 138 percent of the federal poverty level. Additionally, the ACA requires specified rate increases for primary care for two years beginning January 1, 2013 and prohibited California from restricting eligibility primarily for the Medi-Cal and Healthy Families programs before the new coverage requirements went into effect in 2014.

Health care reform will result in a significant net increase of General Fund program costs in fiscal year 2013-14 and beyond. The net impact of health care reform on the General Fund will depend on a variety of factors, including levels of individual and employer participation, changes in insurance premiums, and savings resulting from the reform as beneficiaries in current state-only programs receive coverage through Medi-Cal or the California Health Benefit Exchange (Exchange), also known as Covered California, starting in 2014. The 2014-15 Governor's Budget includes \$124 million General Fund in 2013-14 and \$250.8 million General Fund in 2014-15 for the costs of expanded eligibility under health care reform.

The 2013 Budget Act implemented the optional expansion to include adults up to 138 percent of the federal poverty level using a state-based approach. Under the ACA, the federal government promises to initially pay for 100 percent of the cost of benefits for newly eligible individuals served under the optional expansion; federal funding will gradually decrease to 90 percent by 2020. Other costs, specifically those associated with administrative costs, will be shared 50-50. The state's share of the administrative costs is estimated to be \$65 million in 2014-15. To mitigate against future risks to the General Fund, the legislation that implemented the optional expansion (Chapters 3 and 4, Statutes of 2013-14 First Extraordinary Session) (AB/SB X1 1) requires that reductions in federal funding below 90 percent be addressed in a timely manner through the annual state budget or legislative process. If, prior to January 1, 2018, federal funding under the ACA is reduced to 70 percent or less, the implementation of the optional expansion will cease within 12 months.

As the provider of last resort, counties are responsible for indigent health care. Under the 1991 realignment, the state provides roughly \$1.2 billion to counties to assist them in meeting their obligations. To receive these funds, counties must spend a required maintenance of effort of \$343 million. Many counties spend additional funds on indigent care. Under health care reform, county costs and responsibilities for indigent health care are expected to decrease as uninsured individuals obtain health care coverage. The state, in turn, is bearing increased responsibility for providing care to these newly eligible individuals through the Medi-Cal expansion. Legislation enacted in 2013 (Chapter 24, Statutes of 2013) (AB 85) specifies two mechanisms for determining county savings, depending on how counties currently deliver indigent care. Once determined, these savings will be redirected to fund local human services programs. The 12 public hospital counties and the 12 non-public health/non-County Medical Service Program counties had the option to select one of two mechanisms:

Option 1 – A formula measures actual county health care costs and revenues for Medi-Cal beneficiaries and the uninsured, reflecting historic growth rates and appropriate limits on cost growth. The difference between total revenues and total costs will determine the savings. The state will receive 80 percent of any calculated savings, with the county retaining 20 percent of the savings to

invest in the local health care delivery system or spend on public health activities.

Option 2 – 60 percent of a county’s health realignment allocation plus maintenance-of-effort will be redirected to local human services programs, and the county will retain 40 percent of this funding for providing public health services, to serve the remaining uninsured, or serve other health care needs.

For counties participating in the County Medical Service Program, the Budget provides an alternative that is akin to Option 2.

County health care savings are estimated to be \$300 million in fiscal year 2013-14 and \$900 million in fiscal year 2014-15. Actual savings will depend on the level of realignment revenues for those counties operating under the 60/40 formula and on the various factors used to determine costs and revenues for those counties using the mechanism described in Option 1. Out year savings for all counties will be estimated in January and May, prior to the start of each fiscal year and based on the most recent data available. A true-up process will be used to adjust funding to the extent actual county savings differ from initial estimates. Currently, savings to the counties are estimated to be \$1.3 billion in fiscal years 2015-16 and 2016-17. These savings will provide funding for certain services currently funded by the state.

Chapter 655, Statutes of 2010 (“AB 1602”), and Chapter 659, Statutes of 2010 (“SB 900”), established the Exchange as an independent entity in state government and outline the authorities and responsibilities of the Exchange and its governing board. The Exchange launched its marketplace for individuals and small businesses to purchase health insurance, called Covered California, on October 1, 2013. This entity established requirements for health plans to participate in the Exchange, standards and criteria for selecting health plans to be offered by the Exchange, and required the Exchange to provide an adequate selection of qualified health plans in each region of the state. The federal government initially awarded California \$1 million to fund preliminary planning efforts related to the development of the Exchange. On August 12, 2011, the Exchange received a \$39 million Level I Exchange Establishment grant to help the state design and develop this entity. This was followed by an award of \$196 million in August 2012 for continued support of the Exchange’s start-up, planning, and development activities through June 30, 2013 and an award of \$674 million in January 2013 for continued support through 2014. After 2014, the Exchange must be self-supporting from fees paid by health plans and insurers participating in the Exchange. AB 1602 authorizes the Exchange to assess charges, as a part of premiums, on participating health plans and at rates reasonable to support the ongoing operations of the Exchange and maintain a prudent reserve.

In-Home Supportive Services (IHSS) – On September 17, 2013, the United States Department of Labor released final regulations (effective January 1, 2015) requiring overtime pay for domestic workers, including IHSS providers. Compensation for IHSS providers traveling between multiple recipients, “wait time” that is associated with medical accompaniment, and payment for attending mandatory provider training also is required. These federal regulations have the potential to increase program costs by approximately \$600 million federal and state funds annually.

To control General Fund cost increases while maintaining services to IHSS recipients, the 2014-15 Governor's Budget proposes to: (1) limit provider hours worked to 40 hours within a workweek, (2) require a workweek agreement between recipients and providers, (3) require an IHSS provider back-up system be implemented in each county to ensure IHSS recipients do not experience a gap in services, and (4) require notification and termination of providers who do not comply with the new program requirements. With the restriction of overtime, the new federal requirements will increase General Fund program costs by \$99 million in 2014-15 and \$153.1 million annually thereafter.

California Department of Corrections and Rehabilitation

General – As one of the largest departments in state government, the California Department of Corrections and Rehabilitation (“CDCR”) operates 37 youth and adult correctional facilities and 43 youth and adult camps. The CDCR also contracts for multiple adult parolee service centers and community correctional facilities. The CDCR operates an adult prisoner/mother facility, adult parole units and sub-units, parole outpatient clinics, licensed general acute care hospitals, regional parole headquarters, licensed correctional treatment centers, hemodialysis clinics, outpatient housing units, a correctional training center, a licensed skilled nursing facility, and a hospice program for the terminally ill. The CDCR has six regional accounting offices and leases approximately two million square feet of office space. The CDCR's infrastructure includes more than 42 million square feet of building space on more than 24,000 acres of land (37 square miles) statewide.

Ruling Concerning Prison Population – Pursuant to the ruling issued by a panel of three federal judges (affirmed by the United States Supreme Court), the state was ordered to reduce its prison population to 137.5 percent of the system's design capacity by June 27, 2013. The state has reduced its prison population by an estimated 25,000 inmates due to the realignment of non-serious, non-violent, non-sex offenders from state prisons to local jurisdictions under Chapter 15, Statutes of 2011 (AB 109). On January 7, 2013, the state defendants filed a motion to vacate or modify the three-judge court's population reduction order, citing improvements to its prison healthcare system and the substantial population reductions that have occurred since AB 109 was implemented on October 1, 2011. On April 11, 2013, the three-judge court denied the state defendants' motion, and issued an order requiring the state to reduce overall prison population to 137.5 percent of design capacity by December 31, 2013.

After additional briefing, on June 20, 2013, the three-judge court issued a comprehensive order requiring the state defendants to implement a plan to: increase medical and elderly parole; slow-down the return of certain prisoners housed out-of-state; expand the use of good time credits, prospectively and retroactively, to all prisoners; and release prisoners as needed to meet the population ceiling on December 31, 2013. The state defendants filed requests for a stay of this order and appealed the order to the United States Supreme Court; these requests and the appeal have been denied. On September 12, 2013, Governor Brown signed into law Senate Bill 105, which appropriated \$315 million to be used in different ways depending on whether the December 31st deadline would remain in place.

On February 10, 2014, the three-judge court granted the state's request for a two-year extension of the deadline to meet the 137.5 percent population cap. The court has ordered the

state to comply with the population cap by February 28, 2016 and has also ordered the state to implement the following population reduction measures: 1) increase credit earning for certain non-violent second-strike inmates and minimum custody inmates; 2) create and implement a new parole determination process for non-violent second-strike inmates who have completed 50 percent of their sentence; 3) parole certain inmates serving indeterminate sentences who have already been granted parole but have future parole dates; 4) in consultation with the Receiver's office, finalize and implement an expanded parole process for medically incapacitated inmates and finalize and implement a new parole process for certain elderly inmates; 5) activate a total of 13 reentry hubs within a year of the court's order; 6) pursue expansion of pilot reentry programs with additional counties and local communities; and 7) implement an expanded alternative custody program for women. The court has also ordered that a Compliance Officer be appointed to ensure the state meets the interim benchmarks of 143 percent of design capacity by June 30, 2014, 141.5 percent of design capacity by February 28, 2015, and the final benchmark of 137.5 percent by February 28, 2016. The Compliance Officer will have the authority to order the release of inmates should the state fail to meet any of the benchmarks. The state also agreed not to pursue further court appeals.

In building the 2014-15 Governor's Budget, the Administration had already assumed the court would grant an extension until February 2016 to meet the cap. Based on this assumption, SB 105 expenditures are anticipated to be \$228 million in 2013-14 for a savings of \$87 million. Of the \$87 million in savings, \$81 million will be transferred to the Recidivism Reduction Fund. The Governor's Budget proposes to utilize these funds to expand substance use disorder treatment in state prisons, provide substance use disorder treatment and cognitive behavioral therapy programs at in-state contracted facilities, expand the Integrated Services for Mentally Ill Parolees program, and expand reentry services and sites.

CDCR Budget – The 2014-15 Governor's Budget includes total expenditures of \$9.8 billion (\$9.5 billion General Fund) for CDCR from all funding sources. There is an additional \$865.4 million budgeted for capital outlay expenditures. The CDCR budget includes funding for 60,599 positions at a total cost for salaries and benefits of approximately \$7.4 billion. Lease payments total \$366.4 million, and the remaining funds are budgeted for operating expenses and equipment, insurance, and local assistance.

The 2014-15 Governor's Budget includes savings for CDCR of \$1.5 billion General Fund in fiscal year 2014-15 related to implementation of AB 109. AB 109 shifted responsibility for short-term, lower-level offenders from the state to county jurisdictions. In addition, counties are responsible for community supervision of lower-level offenders upon completion of their prison sentences.

CDCR Population – The average daily adult inmate population is projected to increase from 134,986 in fiscal year 2013-14, to 137,788 in fiscal year 2014-15, an increase of 2,802 inmates. The average daily adult parole population is projected to decrease from 45,934 in fiscal year 2013-14, to 36,652 in fiscal year 2014-15, a reduction of 9,282 adult parolees. The increase in the adult inmate population is due to an increase in new admissions and second striker admissions, while the decline in the adult parole population is related to the passage and implementation of AB 109.

The Division of Juvenile Justice's average daily institutional population is projected to decrease from 711 in fiscal year 2013-14, to 645 in fiscal year 2014-15.

Litigation Concerning Prison Medical Care Services – The federal receiver, the court appointed individual who oversees CDCR's medical operations (the "Receiver"), has plans for the design and construction of additional facilities and improvements to existing facilities for inmates with medical or mental health care needs. All of these projects will be constructed at existing state correctional institutions. See "Prison Construction Program" below.

The 2014-15 Governor's Budget includes \$1.654 billion General Fund for the Receiver's Medical Services and Pharmacy Programs, compared to the 2013 Budget Act, which totaled \$1.628 billion General Fund.

In January 2012, a federal District Court judge ordered California officials to begin planning for the end of the federal Receivership of the state's prison medical programs. The judge, with jurisdiction over the CDCR medical care litigation, cited "significant progress" in improving California's prison medical care and stated that many of the goals of the Receivership had been accomplished. For these reasons, the judge ordered the State and the plaintiffs in the case to prepare a joint report on various aspects of post-Receiver planning. In response to this report, the court ordered the Receiver to work with CDCR to determine when the state will assume responsibility for particular tasks. To date, the Receiver has transitioned health care access units, which provide guarding and transportation for inmates accessing health care services, as well as the responsibility for planning for the activation of new construction that is primarily related to serving the health care needs of inmates. Additional transition planning efforts are underway.

Prison Construction Program – On May 3, 2007, the Governor signed AB 900 (Chapter 7, Statutes of 2007), which provides funding for an expansion of capacity in the state prison system to address housing and health care needs. As last amended on June 27, 2012 (see Chapter 42, Statutes of 2012), AB 900 authorized approximately \$2.1 billion of lease revenue bond financing authority for design and construction of state prison facilities that include the California Health Care Facility and the adjacent DeWitt Nelson Correctional Annex, located in Stockton, and several other medical and mental health projects throughout the state, including the projects in the Health Care Facility Improvement Program. A number of the projects authorized with AB 900 authority have already been completed and occupied and several other projects are in construction and will be completed in 2014 and 2015. Of particular note, the California Health Care Facility began occupancy July 2013, the DeWitt Nelson Correctional Annex is scheduled to begin occupancy in March 2014, and the Central California Women's Facility Enhanced Outpatient Program Treatment and Office Space project is scheduled to begin occupancy in June 2015. In addition, approximately 20 projects in the Health Care Facility Improvement Program are in the design phase and it is anticipated the remaining projects will be initiated during 2014.

The 2012 Budget Act included an additional \$810 million of lease revenue bond financing authority for the design and construction of three new Level II dormitory housing facilities at existing prisons. Two of these new dormitory housing facilities will be located adjacent to Mule Creek State Prison in Ione, and the third will be located adjacent to Richard J.

Donovan Correctional Facility in San Diego. Solicitation of design-build proposals is currently underway. It is anticipated the contracts will be awarded in spring 2014 and construction will be completed in spring 2016. A related provision in the 2012 Budget Act also requires the CDCR to remove all inmates from, cease operations of, and close the California Rehabilitation Center, located in the city of Norco, no later than either December 31, 2016, or six months after construction of these three Level II dorm facilities is completed, whichever is earlier. However, SB 105 suspended this closure indefinitely as the capacity at the Norco facility may be necessary for California's prison population to stay at or below the court-ordered population cap of 137.5 percent of design capacity.

Unemployment Insurance

The Unemployment Insurance ("UI") program is a federal-state program that provides weekly UI payments to eligible workers who lose their jobs through no fault of their own. To be eligible for benefits, a claimant must be able and available to work, seeking work, and be willing to accept a suitable job. The regular unemployment program is funded by unemployment tax contributions paid by employers for each covered worker.

Due to the high rate of unemployment, the employer contributions were not sufficient to cover the cost of the benefits to claimants during the recession. Commencing in January 2009, in accordance with federal law, the state began to fund deficits in the state UI Fund through a federal loan to support benefit payments. The UI Fund deficit was \$10.2 billion at the end of calendar year 2012. Using current economic outlook and unemployment projections, absent changes to the UI Fund financing structure, the deficit is projected to be \$9.7 billion at the end of calendar year 2013 and \$8.8 billion at the end of calendar year 2014. Repayment of principal on this federal UI loan is strictly an employer responsibility, and not a liability of the state's General Fund. To ensure that the federal loan is repaid, when a state has an outstanding loan balance for two consecutive years, the federal government reduces the Federal Unemployment Tax Act ("FUTA") credit it gives to employers. This is equivalent to an increase in the FUTA tax on employers, and has the effect of paying off the federal UI loan. These changes have already started and will increase annually until the fund is returned to solvency.

Pursuant to federal law, if the state is unable to repay the loan within the same year it is taken, state funds must be used to pay the annual interest payments on the borrowed funds. While annual interest payments were waived under the American Recovery and Reinvestment Act of 2010, interest payments of \$303.5 million and \$308.2 million were paid in 2011 and 2012, respectively. Given the condition of the General Fund in those years, loans were authorized from the Unemployment Compensation Disability Fund to the General Fund to pay the UI interest expense. The September 2013 interest payment of \$259 million was paid from the General Fund. The Budget proposes \$231.6 million from the General Fund to make the 2014 interest payment. Interest will continue to accrue and be payable annually until the principal on the UI loan is repaid. Pursuant to federal law, the General Fund is not liable for repayment of the principal of this loan, which will be done over time by reducing federal tax credits to employers in the state.

The interest due after fiscal year 2014-15 will depend on a variety of factors, including the actual amount of the federal loan outstanding (which in turn will depend on the rate of

unemployment, employer contributions to the UI Fund, and any state or federal law changes relating to the funding of the program) and the interest rate imposed by the federal government. In an effort to identify preferred alternatives to meet annual federal interest obligations, repay the federal loan, and return the state's UI Fund to solvency, the Secretary for Labor and Workforce Development convened a series of meetings to bring together key stakeholders, including business and labor. The Administration intends to continue working with these stakeholders to develop a solution. The Budget identifies a framework for solvency which identifies goals and principles to guide future discussions.

Retiree Health Care Costs

In addition to a pension, described in the following section "PENSION TRUSTS," the state also provides postemployment health care and dental benefits to its employees and their spouses and dependents, when applicable, and, except as otherwise described below, utilizes a "pay-as-you-go" funding policy. These are sometimes referred to as "Other Postemployment Benefits" or "OPEB."

As of June 30, 2012, approximately 157,100 retirees were enrolled to receive health benefits and 130,700 to receive dental benefits. Generally, employees vest for those benefits after serving 10 years with the state. With 10 years of service credit, employees are entitled to 50 percent of the state's full contribution. This rate increases by 5 percent per year and with 20 years of service, the employee is entitled to the full 100/90 formula (as described below). Additional information on the State's OPEB plan can be found in the Comprehensive Annual Financial Report for the fiscal year ended June 30, 2012 included as APPENDIX F to this Official Statement.

Pursuant to the Governmental Accounting Standards Board Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions, the state now reports on its liability for postemployment healthcare as well as other forms of postemployment benefits, such as life insurance, in its annual financial reports. The long-term costs for other postemployment benefits may negatively affect the state's financial reports and impact its credit rating if the state does not adequately manage such costs.

On March 6, 2014, the State Controller's Office released the state's latest OPEB actuarial valuation report by the private actuarial firm, Gabriel, Roeder, Smith & Company, which was tasked with calculating the state's liability for these benefits. The report was based on a variety of data and economic, demographic and healthcare trend assumptions described in the report. The primary assumption influencing Annual OPEB Costs and the Actuarial Accrued Liability ("AAL") is the assumed rate of return or discount rate on assets supporting the retiree healthcare liability. Based on PMIA's historical returns, investment policy and expected future returns, a discount rate of 4.25 percent was selected for the pay as you-go funding policy. The economic assumptions such as the price and wage inflation are assumed to be 2.75 percent and 3 percent, respectively. The actuarial valuation contained in the report covers the cost estimates for existing employees, retirees and dependents. The main objective of the report was to estimate the AAL, which is the present value of future retiree healthcare costs attributable to employee service earned in prior fiscal years.

The report looked at three different scenarios: (i) continuation of the “pay-as-you-go” policy; (ii) a “full funding” policy under which assets would be set aside to prepay the future obligations, similar to the way in which pension obligations are funded, and (iii) a “partial funding” policy, a hybrid of the two scenarios. According to the actuarial valuation as of June 30, 2013, the pay-as-you go funding policy results in an unfunded AAL of \$64.57 billion as of June 30, 2013. Additionally, the pay-as-you go funding policy results in an annual OPEB cost of \$5.12 billion, estimated employer contributions of \$1.78 billion and an expected net OPEB obligation of \$19.46 billion for fiscal year 2013-14. The annual required contribution for fiscal year 2014-15 is estimated at \$5.08 billion.

If the previous assumptions had been exactly realized during the year, the actuarial liability would have increased to \$67.32 billion as of June 30, 2013. The key factors contributing to a \$2.74 billion change in expected actuarial liabilities had the previous assumptions been realized are:

Favorable healthcare claims experience and plan design changes, resulting in a decrease in actuarial liabilities of approximately \$5.71 billion.

Changes in demographic experience (including more members retiring, retiring earlier, and living longer than assumed) caused actuarial liabilities to increase by \$0.25 billion.

Changes in OPEB related assumptions and methods (inflation assumptions changing from 3.00 to 2.75 percent, impacting the discount rate, wage inflation, and salary increases) increased actuarial liabilities by \$2.72 billion.

The valuation depended primarily on the interest discount rate assumption used to develop the present value of future benefits and on the assets available to pay benefits. The discount rate of 4.25 percent represents the long-term expectation of the earnings on the state’s General Fund, which is invested in short-term securities in the PMIA. The State Controller’s Office plans to issue an actuarial valuation report annually.

The following table is the historic annual OPEB cost summary and the projected schedule of funding progress as of the valuation date for the five fiscal years indicated below:

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TABLE 23
OPEB Pay-As-You-Go Funding
Fiscal Years 2009-10 to 2013-14

(Dollars in Billions)

Fiscal Year	Annual OPEB Cost	Net Employer Contribution	Percentage of Annual OPEB Cost Contribution	Net OPEB Obligation	Unfunded Actuarial Accrued Liability^(b)	Unfunded Actuarial Accrued Liability as Percent of Payroll^(b)
2009-10	\$3.93	\$1.37	35%	\$7.25	\$59.91	341%
2010-11	4.21	1.58	38	9.88	62.14	345
2011-12	4.74	1.72	36	12.91	63.84	341
2012-13	4.99	1.78	36	16.12	64.57	358
2013-14 ^(a)	5.12	1.78	35	19.46	N/A	N/A

^(a) Net employer contribution and Net OPEB Obligation estimated for fiscal year ending June 30, 2014.

^(b) Amounts are projected as of the valuation date.

Source: State of California OPEB Valuation as of June 30, 2013.

The following table illustrates the state's budget for postemployment benefits from fiscal years *2007-08 to 2014-15* and does not reflect any future liability for current employees or annuitants. It is anticipated that these costs will continue to grow in the future. The employer contribution for health premiums maintains the average 100/90 percent contribution formula established in the Government Code. Under this formula, the state averages the premiums of the four largest health benefit plans in order to calculate the maximum amount the state will contribute toward the retiree's health benefits. The state also contributes 90 percent of this average for the health benefits of each of the retiree's dependents. CSU employees fully vest for the 100/90 formula at 5 years of service. As noted below, employees in bargaining unit 12, hired after January 1, 2011, are subject to a longer vesting period.

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TABLE 24
Actual Costs/Budget for Other Postemployment Benefits
Fiscal Years 2007-08 through 2014-15
(Dollars in Thousands)

Fiscal Year	State Employees All Funds^(c)	State Employees General Fund	CSU Employees All General Fund	Total Contributions All Funds	Total General Fund Contributions
2007-08	1,114,317	1,051,486	N/A	1,114,317	1,051,486
2008-09	1,183,495	1,146,932	N/A	1,183,495	1,146,932
2009-10	1,182,497	1,145,934	N/A	1,182,497	1,145,934
2010-11	1,386,839	1,351,008	N/A	1,386,839	1,351,008
2011-12	1,504,928	1,466,528	N/A	1,504,928	1,466,528
2012-13	1,365,234	1,337,089	222,135	1,587,369	1,359,224 ^(b)
2013-14 ^(a)	1,420,250	1,416,242	245,794	1,666,044	1,662,036
2014-15 ^(a)	1,559,336	1,553,336	270,144	1,829,480	1,823,480

(a) Estimated Contributions.

(b) Contributions for post-employment benefits are included for all years displayed in this table. However, beginning in 2012-13, CSU contributions are split out and identified separately.

(c) "Pay-as-you-go" contributions from General Fund and Public Employee's Contingency Reserve Fund.

Source: State of California, *Department of Finance*.

Three state employee bargaining units have agreements which provide for some prefunding of OPEB liabilities. These units represent a little less than 10 percent of total state unionized employees.

In accordance with state law, the Bureau of State Audits periodically identifies what it believes to be "high risk" issues facing the state. The funding of OPEB liabilities has been identified as a high-risk issue in the California State Auditor Report 2013-601 dated September 2013.

PENSION TRUSTS

General

The principal retirement systems in which the state participates or contributes funds to are the California Public Employees' Retirement System ("CalPERS") and the California State Teachers' Retirement System ("CalSTRS"). The assets and liabilities of the funds administered by CalPERS and CalSTRS are included in the financial statements of the state as fiduciary funds. A summary description of CalPERS and CalSTRS is set forth in Note 24 (and the Schedule of Funding Progress included in the Required Supplementary Information) to the Audited Basic Financial Statements of the State of California for the Year Ended June 30, 2012. See "FINANCIAL STATEMENTS."

The University of California ("UC") maintains a separate retirement system. From fiscal years 1990-91 through 2011-12, no amounts from the state's General Fund directly contributed to UC's retirement system. The 2012 Budget Act and Chapter 31 of the Statutes of 2012 provided \$89.1 million in state General Fund appropriations for UC's employer retirement

contributions for fiscal year 2012-13; this funding does not constitute a state obligation to provide funding after fiscal year 2012-13 for additional UC employer retirement costs.

The 2013 Budget Act did not allocate any of UC's appropriation specifically to fund its employer retirement costs, however, the 2013 Budget Act and Chapter 50 of the Statutes of 2013 shifted funding for UC's general obligation and lease revenue bond debt service into UC's main support appropriation, authorized UC to restructure its debt, and required UC to use any savings from restructuring of debt to reduce the existing unfunded liability of the UC's retirement plan. Information about this system may be obtained directly from UC. The 2014-15 Governor's Budget does not allocate any of UC's appropriation specifically to fund their employer retirement costs.

As described below, the obligation of the state to make payments to CalPERS and CalSTRS to fund retirement benefits constitutes a significant financial obligation. CalPERS and CalSTRS each currently have unfunded liabilities in the tens of billions of dollars. Retirement-related costs payable from the General Fund are expected to increase in the foreseeable future. The actual amount of such increases will depend on a variety of factors, including but not limited to investment returns, actuarial assumptions, experience, retirement benefit adjustments and, in the case of CalSTRS, statutory changes to contribution levels.

This section contains certain information relating to CalPERS and CalSTRS. The information is primarily derived from information produced by CalPERS and CalSTRS, their independent accountants and their actuaries. The state has not independently verified the information provided by CalPERS and CalSTRS and makes no representations nor expresses any opinion as to the accuracy of the information provided by CalPERS and CalSTRS.

The comprehensive annual financial reports of CalPERS and CalSTRS are available on their websites at www.calpers.ca.gov and www.calstrs.ca.gov, respectively. The CalPERS and CalSTRS websites also contain the most recent actuarial valuation reports, as well as other information concerning benefits and other matters. Such information is not incorporated by reference herein. The state cannot guarantee the accuracy of such information. Actuarial assessments are "forward-looking" information that reflect the judgment of the fiduciaries of the pension plans, and are based upon a variety of assumptions, one or more of which may not materialize or be changed in the future. Actuarial assessments will change with the future experience of the pension plans.

On June 25, 2012, the Governmental Accounting Standards Board ("GASB") approved two new standards with respect to pension accounting and financial reporting standards for state and local governments and pension plans. The new standards are set forth in GASB Statements 67 and 68 and will replace GASB Statement 27 and most of GASB Statements 25 and 50. The changes will impact the accounting treatment of pension plans in which state and local governments participate. Major changes include: 1) the inclusion of unfunded pension liabilities on the government's balance sheet (currently, such unfunded liabilities are typically included as notes to the government's financial statements); 2) more components of full pension costs will be shown as expenses regardless of actual contribution levels; 3) lower actuarial discount rates will be required to be used for underfunded plans in certain cases for purposes of the financial statements; 4) closed amortization periods for unfunded liabilities will be required to be used for

certain purposes of the financial statements; and 5) the difference between expected and actual investment returns will be recognized over a closed five-year smoothing period.

In addition, GASB Statement 68 states that, for pensions within the scope of the statement, a cost-sharing employer that does not have a special funding situation is required to recognize a net pension liability, deferred outflows of resources, deferred inflows of resources related to pensions, and pension expense based on its proportionate share of the net pension liability for benefits provided through the pension plan. Because the accounting standards do not require changes in funding policies, the full extent of the effect of the new standards on CalPERS and CalSTRS is not known at this time. The reporting requirements for pension plans will take effect for the fiscal year beginning mid-2013 and the reporting requirements for government employers will take effect for the fiscal year beginning mid-2014.

Pension Reform

Chapter 296, Statutes of 2012 (AB 340), a comprehensive pension reform package affecting state and local government, increased the retirement age and lowered retirement benefits for most new state and local government employees hired on or after January 1, 2013. AB 340, known as the Public Employees' Pension Reform Act of 2013 ("PEPRA") also includes provisions to increase current employee contributions. Though PEPRA covers most public employees in state government, cities, counties, special districts, school districts, and community colleges, the following discussion relates only to PEPRA's impact on state employee retirement. PEPRA excludes judges, the University of California, and charter cities with independent pension systems from the new retirement plans; however, newly elected or appointed judges would be subject to the new cost-sharing provisions described below.

In a preliminary actuarial analysis, CalPERS noted savings to the state of \$10.3 billion to \$12.6 billion over the next 30 years due primarily to increased employee contributions and, as the workforce turns over, lower benefit formulas that will gradually reduce normal costs. PEPRA also directs state savings from additional employee contributions to be used toward additional payments on the state's unfunded liability, subject to Budget Act approval. The 2014-15 Governor's Budget includes an additional \$108.4 million (\$73.8 million General Fund) directed toward the state's unfunded pension liability to reflect the savings resulting from increased employee contributions under PEPRA.

Other provisions reduce the risk of the state incurring additional unfunded liabilities, including prohibiting retroactive benefits increases, generally prohibiting contribution holidays, and prohibiting purchases of additional non-qualified service credit ("air time").

Key changes to retirement plans affecting the state include:

New, lower defined-benefit formulas that increase retirement ages for new public employees hired on or after January 1, 2013.

For new employees, a cap on pensionable income in the 2013 calendar year of \$113,700, or \$136,440 (for employees not in Social Security). Annual increases on the cap would be limited to the Consumer Price Index for All

Urban Consumers. As of January 1, 2014, the cap on pensionable income was adjusted to \$115,064, or \$138,077 (for employees not in Social Security).

A standard that employees pay at least 50 percent of normal costs.

Establishes increases for current state civil service and related excluded employees who are not contributing at least half of normal costs.-

CSU and judicial branch employees hired on or after January 1, 2013 will pay at least 50 percent of the normal cost or the current contribution rate of similarly situated employees, whichever is greater.

Chapter 528, Statutes of 2013, (SB 13) made clarifying and technical amendments to PEPRA which authorizes CSU, on or after January 1, 2019, to impose higher employee contribution rates on CSU members hired before January 1, 2013. SB 13 also directs savings from increased CSU employee contributions to be retained by the university.

Costs for OPEB are not addressed in PEPRA, however, later retirement ages will help reduce OPEB liabilities in the long term.

Provisions in PEPRA affecting the CalSTRS system do not change the state's statutory contribution rate and will not likely have a material effect on state contributions in the short term. However, potential additional employee contributions, limits on pensionable compensation, and higher retirement ages for new members will reduce pressure on the system's unfunded liabilities and potentially state contribution levels in the long term.

On February 14, 2013, CalSTRS submitted a report to the Legislature on the funding of the Defined Benefit Program (referred to in the state's 2012 Financial Statements and in this APPENDIX A as the "DB Program") in response to Senate Concurrent Resolution 105 ("SCR 105"). SCR 105 encouraged CalSTRS, "in consultation with affected stakeholders, including, but not limited to, the Department of Finance and organizations representing members and school employers, to develop at least three options to address the long-term funding needs of the DB Program in a manner that allocates any increased contributions among the members of the system, school employers, and the state, consistent with the contractual rights of existing members, and to submit those options to the Legislature before February 15, 2013." SCR 105 further provided that "It is the intent of the Legislature to enact legislation during the 2013-14 Regular Session that addresses the long-term funding needs of the Defined Benefit Program." There was no such legislation considered.

The report stated that "the definitive approach to addressing the long-term funding needs of the DB Program is to fully fund the program over a period of 30 years or less" and that "if implemented on July 1, 2014, the total contribution rate from all sources would have to increase by the equivalent of a projected 15.1% of compensation to fully fund the program in 30 years." The report stated that "it is projected that such a change would require an increased initial total annual contribution at that time of about \$4.5 billion from all combined sources." The report also discussed the options of establishing a lesser funding target or increasing the amortization

period (both of which would not require similarly large contributions from combined sources). The report stated that “a delay in addressing the DB Program funding shortfall places the program at greater risk, particularly if there is another substantial market downturn.”

The 2014-15 Governor’s Budget does not include increased state contributions to CalSTRS beyond current statutory requirements; however, it does outline the Administration’s intent to begin working with stakeholders of CalSTRS to develop a plan of shared responsibility to achieve a fully-funded, sustainable teacher pension system within 30 years. It is expected that this plan will be part of the 2015-16 budget.

On January 29, 2014, Speaker of the Assembly, John Perez, and Assembly Member Rob Bonta announced their intention to implement a long-term solution for the CalSTRS funding shortfall during the current legislative session. Speaker Perez stated the goal of any funding solution would be to fully fund the system under a plan of shared responsibility between school districts, the state, and teachers.

On February 19, 2014 the Assembly Committee on Public Employees, Retirement and Social Security held the first in a planned series of hearings to address CalSTRS’ long-term funding needs. At this informational hearing, Assembly Member Bonta reiterated the committee’s goal to enact a funding plan for CalSTRS in the current legislative session which would fully fund the pension plan within several decades. In addition to updating the committee on the current status of the pension system relative to SCR 105, CalSTRS testified that absent any changes to contribution rates or liabilities, the unfunded liability will continue to grow by approximately \$22 million per day and the system will deplete its assets as early as 2043. Additionally, CalSTRS stated that after incorporating the impact of the 13.8 percent investment return earned in 2012-13, the system would require additional funding equivalent to 14.2 percent of payroll (at this time about \$4.2 billion) per year to fully fund the system within 30 years.

CalPERS

General

At June 30, 2013, CalPERS administered a total of 13 funds, including four defined benefit retirement plans: the Public Employees’ Retirement Fund (“PERF”), the Legislators’ Retirement Fund (“LRF”), the Judges’ Retirement Fund (“JRF”), and the Judges’ Retirement Fund II (“JRF II”). (These plans, as well as the other plans administered by CalPERS, are described in the comprehensive financial reports of CalPERS, which can be found on CalPERS’ website at www.calpers.ca.gov. Such information is not incorporated by reference herein.) The PERF, LRF, JRF, and JRF II are defined benefit pension plans which provide benefits based on members’ years of service, age, final compensation, and benefit formula. In addition, benefits are provided for disability, death, and survivors of eligible members or beneficiaries. Certain summary information concerning PERF is set forth below. Certain summary information concerning LRF, JRF, and JRF II is set forth at the end of this section.

CalPERS is administered by a 13-member Board of Administration (the “CalPERS Board”), that includes the State Controller, State Director of the Department of Human Resources, and the State Treasurer, who serve ex officio. The other CalPERS Board members

include a member elected by school employees, a member elected by retirees, a member elected by state employees, a member elected by public agency employees, a member designated by the State Personnel Board, a public representative appointed jointly by the Speaker of the Assembly and the Senate Rules Committee, an official of a life insurer appointed by the Governor, an elected local official appointed by the Governor, and two members elected by all employees.

PERF

PERF is a multiple-employer defined benefit retirement plan. In addition to the state, employer participants at June 30, 2013 included 1,580 public agencies and schools (representing more than 2,500 entities). CalPERS acts as the common investment and administrative agent for the member agencies. The state and schools (for “classified employees,” which generally consist of school employees other than teachers) are required by law to participate in PERF. Other public agencies can elect whether or not to participate in PERF or administer their own plans. Members of PERF generally become fully vested in their retirement benefits earned to date after five years of credited service. Separate accounts are maintained for each employer participating in PERF, and separate actuarial valuations are performed for each individual employer’s plan to determine the employer’s periodic contribution rate and other information for the individual plan, based on the benefit formula selected by the employer and the individual plan’s proportionate share of PERF assets.

Unless otherwise specified, the information relating to PERF provided in this section relates only to state employees participating in PERF. State employees include Executive Branch, California State University, Judicial, and Legislature employees.

Members

Benefits to state employees are paid according to the category of employment and the type of benefit coverage provided by the state. All employees in a covered class of employment who work on a half-time basis or more are eligible to participate in PERF. The five categories of membership applicable to state employees are set forth below. Certain of the categories also have “tiers” of membership. It is up to the employee to select his or her preferred membership tier. Different tiers may have different benefits, as well as different employee contribution requirements. The member categories are as follows:

Miscellaneous Members – staff, operational, supervisory, and all other eligible employees who are not in special membership categories.

Safety Members – employees whose principal duties are in active law enforcement or fire prevention and suppression work but are not defined as a State Peace Officer/Firefighter Member, or who occupy positions designated by law as Safety Member positions.

State Industrial Members – employees of the California Department of Corrections and Rehabilitation who have the same service retirement and other benefits as Miscellaneous Members, but who also have industrial death and disability benefits under certain limited circumstances.

State Peace Officer/Firefighter Members – employees who are involved in law enforcement, firefighting and fire suppression, public safety, protective services, or the management and supervision thereof, whose positions are defined as State Peace Officer/Firefighter Members in the Government Code or by the Department of Human Resources.

Patrol Members – California Highway Patrol officers and their related supervisors and managers.

The following table reflects the number of state employee members of PERF as of June 30, 2012 and June 30, 2013. (PERF’s fiscal year commences July 1 and ends June 30 of the following year).

TABLE 25
PERF Membership (State Employees) as of June 30, 2012 and 2013

<u>Category</u>	<u>2012</u>	<u>2013</u>
Retirees	169,657	175,851
Survivors and Beneficiaries	26,567	28,785
Active Members	244,171	243,620
Inactive Members	<u>91,428</u>	<u>90,463</u>
Total	531,823	538,719

Source: CalPERS Comprehensive Annual Financial Report for Fiscal Years ended June 30, 2011 and June 30, 2012.

Retirement Benefits

For state employees, annual benefits depend on the particular employee’s employment category and are generally determined by taking into account years of service credit, final compensation, and age of retirement. Depending on the employment category, annual benefits generally range from 2 percent of final compensation (generally meaning the average pay rate and special compensation over the last one year or three consecutive years of employment, unless the member elects a different period with a higher average) at age 55 for each year of service credit (applicable to Miscellaneous and State Industrial category members) to 3 percent of final compensation for each year of service for retirement at age 50 (for State Peace Officer/Firefighter category members). Annual benefits are also subject to annual cost of living adjustments (generally ranging from 2-3 percent) and an additional adjustment intended to preserve the “purchasing power” of the benefit. Benefits also generally include disability and death benefits. A detailed description of the benefits payable by PERF to state employees is set forth in CalPERS actuarial valuations.

Legislation enacted in October 2010 as part of the state’s budget for fiscal year 2010-11 (SB 22, Chapter 3, Sixth Extraordinary Session of 2010) (“SBX6 22”) made changes to the retirement formula for state employees hired after January 15, 2011, unless an earlier date was agreed upon in a collective bargaining agreement. Generally, the formula for receiving full retirement benefits was restored to the provisions in effect prior to 1999, when a law increased

the percentage formula and reduced the age at which employees could obtain maximum benefits; these formulas vary depending on the category of employment.

SBX6 22 also addressed the problem of pension “spiking” by generally requiring the retirement formula for future employees not currently in the three-year formula to be based on an average of pay in three consecutive years, rather than being based on the single highest year’s pay. These reforms will not significantly impact state retirement costs until many years in the future. However, there are also current savings from most existing and future employees contributing a greater percentage, ranging from two to five percent, of their salaries toward future pension benefits. These increases were collectively bargained and extended to most non-represented employees.

AB 340 is a comprehensive pension reform package impacting state and local governments that increased retirement age and reduced benefits for most new employees. See “PENSION TRUSTS – Pension Reform.”

The following table shows the amount of benefits paid from PERF for fiscal years 2006-07 through 2011-12.

TABLE 26
PERF (State Only)
Schedule of Benefits Paid
(Dollars in Millions)

<u>Fiscal Year</u>	<u>Amount of Benefits Paid</u>
2006-07	\$4,352
2007-08	4,741
2008-09	5,037
2009-10	5,485
2010-11	6,017
2011-12	6,711

Source: CalPERS State and Schools Actuarial Valuation for fiscal years ended June 30, 2007 through June 30, 2012.

Member Contributions

The benefits for state employees in PERF are funded by contributions from members, the state, and earnings from investments. Member and state contributions are a percentage of applicable member compensation. Member contribution rates are defined by law and vary by bargaining units within the same employee classification. The required contribution rates of active plan members are based on a percentage of salary in excess of a base compensation amount ranging from \$0 to \$863 monthly, and range from 1.5 to 12 percent.

Actuarial Methods

Generally, the ultimate cost that PERF incurs is equal to benefits paid plus the expenses resulting from administration. These costs are paid through contributions to the plan and

investment earnings on PERF's assets. Using the state plan's schedule of benefits, member data, and a set of actuarial assumptions, CalPERS' actuary estimates the cost of the benefits to be paid. Then, using the actuarial funding method determined by CalPERS (as described below), the actuary allocates these costs to the fiscal years within the employee's career. CalPERS' financial objective is to fund in a manner which keeps contribution rates approximately as a level percentage of payroll from generation to generation, while accumulating sufficient assets over each member's working career.

The primary funding method used to accomplish this objective is the "Entry Age Normal Cost Method." New GASB standards will require all states and local governments with pension liabilities to use the Entry Age Normal Cost Method beginning in fiscal year 2014-15 if they are not already doing so. Annual actuarial valuations are performed as of each June 30. Information through the most recent valuation date of June 30, 2012 is set forth below. According to CalPERS, the actuarial assumptions and methods used by CalPERS for funding purposes meet the current parameters set for disclosures presented in the Financial Section by GASB Statements 25 and 27.

Under the Entry Age Normal Cost Method, projected benefits are determined for all members. For active members, liabilities are spread in a manner that produces level annual costs as a level percent of pay in each year from the age of hire (entry age) to the assumed retirement age. The cost allocated to the current fiscal year is called the "normal cost." The Actuarial Accrued Liability ("AAL") for active members is then calculated as the portion of the total cost of the plan allocated to prior years.

The AAL for members currently receiving benefits, for active members beyond the assumed retirement age, and for inactive members entitled to deferred benefits is equal to the present value of the benefits expected to be paid. No normal costs are applicable for these participants. The excess of the total AAL over the value of plan assets is called the unfunded actuarial accrued liability. The required contribution is then determined by adding the normal cost and an amortization of the unfunded liability as a level percentage of assumed future payroll.

With respect to CalPERS, the unfunded liability is broken down into components, or bases, according to their date of origin and the cause that gave rise to that component. A component of the unfunded liability that arose due to a change in plan provisions or in actuarial methods or assumptions is separately tracked and amortized over a declining 20-year period. The actuarial assumptions discussed below are used to determine projected benefits. The effect of differences between those assumptions and the actual experience of the plan is calculated each year when the annual actuarial valuation is performed. These differences are actuarial gains or losses.

Gains and losses are tracked separately and amortized over a rolling 30-year period (except as described below with respect to gains and losses in fiscal years 2008-09 through 2010-11). A maximum 30-year amortization payment on the entire unfunded liability is enforced on the amortization methods described above. In addition, when the amortization methods described above result in either mathematical inconsistencies or unreasonable actuarial results, all unfunded liability components are combined into a single base and amortized over a period of

time, as determined by the CalPERS Chief Actuary. There is a minimum employer contribution equal to normal cost, less 30-year amortization of surplus (negative unfunded liability), if any.

In 2009, the CalPERS Board adopted a change to the amortization policy, described in the following section. This change resulted in all actuarial gains and losses for fiscal years 2008-09, 2009-10, and 2010-11 to be amortized over a fixed 30-year period instead of a rolling 30-year period. The rolling 30-year period for amortization resumed with actuarial gains and losses for fiscal year 2011-12.

In April of 2013, the CalPERS Board adopted new amortization and smoothing methodologies. The new methodologies replace the current 15-year asset-smoothing policy with a 5-year direct-rate smoothing process and replace the current 30-year rolling amortization of actuarial gains and losses with a 30-year fixed amortization period. See the following section for further detail.

Actuarial Valuation; Determination of Required Contributions

The required state contributions to PERF are determined on an annual basis by the CalPERS Chief Actuary. The actuary uses demographic and other data (such as employee age, salary, and service credits) and various assumptions (such as estimated salary increases, interest rates, employee turnover, and mortality and disability rates) to determine the amount that the state must contribute in a given year to provide sufficient funds to PERF to pay benefits when due. The actuary then produces a report, called the “actuarial valuation,” in which the actuary reports on the assets, liabilities, and required contribution for the following fiscal year. State law requires the state to make the actuarially-required contribution to PERF each year.

A portion of the actuarial valuations performed by CalPERS actuaries are audited each year by an independent actuarial firm. The actuarial valuations specific to state employees are audited every three years. The most recent audit was for the June 30, 2009 actuarial valuation and was completed in the fall of 2010. The audit for the June 30, 2012 actuarial valuation is expected to be completed in March of 2014.

The market value of assets measures the value of the assets available in the pension plan to pay benefits. The actuarial value of assets is used to determine the required employer contributions. Various methods exist for calculating the actuarial value of assets. Since 2005, CalPERS has recognized investment gains and losses on the market value of assets equally over a 15-year period when determining the actuarial value of assets. (This is referred to as “smoothing.”) The recognized portion is added to the gains and losses and (except as described herein) is amortized over a rolling 30-year period (as described herein under “Actuarial Methods”). This is currently an approved method for determining actuarial value of assets under GASB Statements 25 and 27.

Asset smoothing delays recognition of gains and losses, however, thereby providing an actuarial value of assets that does not reflect the market value of pension plan assets at the time of measurement. As a result, presenting the actuarial value of assets as determined using “smoothing” might provide a more or less favorable presentation of the current financial position of a pension plan than would a method that recognizes investment gains and losses annually. As

discussed under the caption “PENSION TRUSTS – General,” beginning in fiscal year 2014-15, GASB Statement 68 will require state and local governments with pension liabilities to recognize the difference between expected and actual investment returns over a closed 5-year period. CalPERS will continue to set contributions based on an actuarial value basis until fiscal year 2015-16, at which time CalPERS will implement a new direct-rate smoothing policy as described below.

In addition to the use of “smoothing,” as described above, when CalPERS sets contribution rates, the actuarial value of assets generally cannot be more than 120 percent of the market value or less than 80 percent of the market value (referred to as the “corridor”). Any asset value changes outside these ranges will be recognized immediately, and will result in a greater impact on future state contribution rates. However, in 2009 CalPERS adjusted the “corridor” to mitigate the effects of a negative 24 percent fiscal year 2008-09 investment loss.

According to CalPERS, the 3-year phase-in of the fiscal year 2008-09 investment loss is achieved by temporarily relaxing the constraints on the smoothed value of assets. Previously, the actuarial value of assets could not be more than 120 percent of the market value or less than 80 percent of the market value. Under the 3-year phase in, assets are treated as follows:

1. For the June 30, 2009 actuarial valuations of the State plans setting the contribution requirements for fiscal year 2010-11, the actuarial value of assets cannot be more than 140 percent of the market value or less than 60 percent of the market value.

2. For the June 30, 2010 actuarial valuations of the State plans setting the contribution requirements for fiscal year 2011-12, the actuarial value of assets cannot be more than 130 percent of the market value or less than 70 percent of the market value.

3. For the June 30, 2011 actuarial valuations of the State plans setting the contribution requirements for fiscal year 2012-13, the actuarial value of assets cannot be more than 120 percent of the market value or less than 80 percent of the market value.

Lastly, the asset loss outside of the 80 – 120 percent corridor will be isolated, and paid down with a fixed and certain 30-year amortization schedule. By utilizing a fixed and certain 30-year payment schedule, these losses will be paid in full at the end of 30 years, and will be independent of any investment gain/loss experienced by the remaining portfolio as a whole.

The use of “smoothing” and the “corridor” described above will mitigate short term increases in the state’s required annual contribution. While this will limit extreme increases in the state’s required annual contribution to CalPERS in the near term, absent investment returns significantly over and above the 7.5 percent assumed by CalPERS, it is expected to result in significantly higher required contributions in future fiscal years.

Depending on actual investment returns and other factors, the state’s required annual contribution to PERF could increase significantly. The contribution, not including CSU, is estimated to be \$3.5 billion for fiscal year 2014-15, approximately \$1.8 billion of which is payable from the General Fund. In addition, CSU’s contribution is estimated to be approximately \$477.7 million for fiscal year 2014-15, approximately \$477.5 million of which is payable from the General Fund.

At the April 16 and 17, 2013, meetings, the CalPERS Board approved a plan to replace the current 15-year asset-smoothing policy with a 5-year direct-rate smoothing process and replace the current 30-year rolling amortization of unfunded liabilities with a 30-year fixed amortization period. The Chief Actuary stated that the approach provides a single measure of funded status and unfunded liabilities, less volatility in extreme years, a faster path to full funding, and more transparency to employers about future contribution rates. These changes will accelerate the repayment of unfunded liabilities (including 2008-09 investment losses) of the state plans in the near term. Under the CalPERS Board action, actual rates for the state will not be set using the new methods until fiscal year 2015-16, reflected in the June 30, 2014 valuation. The impact of the new amortization and smoothing policies are estimated to increase state retirement contributions (including CSU) by \$200 million in fiscal year 2015-16 and \$400 million in fiscal year 2016-17, roughly half of those increases coming from the General Fund.

Actuarial Assumptions

The CalPERS Chief Actuary considers various factors in determining the assumptions to be used in preparing the actuarial report. Demographic assumptions are based on a study of the actual history of retirement, rates of termination/separation of employment, years of life expectancy after retirement, disability, and other factors. This experience study is generally done once every four years. The most recent experience study was completed in 2010 in connection with the preparation of actuarial recommendations by the CalPERS Chief Actuary as described below. The following table sets forth certain economic actuarial assumptions for the fiscal years ended June 30, 2009 through June 30, 2012.

TABLE 27
Certain Actuarial Assumptions Utilized for PERF

<u>Actuarial Assumption</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>
Investment Returns	7.75%	7.75%	7.50%	7.50%
Inflation	3.00	3.00	2.75	2.75
Salary Increase (Total Payroll)	3.25	3.25	3.00	3.00

Source: CalPERS State and Schools Actuarial Valuation for fiscal years ended June 30, 2009 through June 30, 2012.

On February 20, 2014, the CalPERS Board of Administration adopted new mortality and retirement assumptions as part of a regular review of demographic experience. Key assumption changes included longer post-retirement life expectancy, earlier retirement ages, and higher-than-expected wage growth for State Peace Officers/Firefighters and California Highway Patrol. The impact of the assumption changes will be phased in over three years, with a twenty year amortization, beginning in 2014-15.

The Department of Finance estimates these changes will incrementally increase state retirement contributions by an additional \$430.1 million (\$254.2 General Fund) in 2014-15, an additional \$267.2 million (\$138.0 million General Fund) in 2015-16, and an additional \$281.1 million (\$152.7 million General Fund) in 2016-17. Since the assumption changes will be fully phased-in by 2016-17, the cumulative additional retirement contributions will be \$978.5 million

(\$545.0 million General Fund). According to CalPERS, the assumption changes are estimated to increase the system's unfunded liability by approximately \$9.0 billion in 2014-15. These estimates only reflect the new assumptions and do not include other natural changes such as actual payroll and investment performance. In April 2014, the CalPERS Board is anticipated to adopt the June 30, 2013 actuarial valuation, which will include the final retirement rates for 2014-15 and the unfunded liability.

Funding Status

The following table sets forth the schedule of funding progress relating to the state's participation in PERF as of the ten most recent actuarial valuation dates. Funding progress is measured by a comparison of the state's share of PERF assets to pay state employee benefits with plan liabilities.

As reflected in the actuarial valuation report for the fiscal year ended June 30, 2012, the investment return for the PERF in fiscal year 2011-12 was 0.1 percent. As a result of this investment return, the funded ratio on an MVA basis was approximately 66.1 percent as of June 30, 2012, as compared to approximately 70.3 percent as of June 30, 2011, and the unfunded liability was approximately \$45.5 billion on an MVA basis as of June 30, 2012, as compared to approximately \$38.5 billion on an MVA basis as of June 30, 2011.

At the CalPERS Finance and Administration Committee meeting on June 18, 2013, staff presented the employer retirement contribution rates and other actuarial information to be incorporated into the June 30, 2012 Actuarial Valuation. The full CalPERS Board adopted these items on June 19, 2013. The full June 30, 2012 Actuarial Valuation was released on September 27, 2013.

The actuarial report for the fiscal year ended June 30, 2012 can be found on the CalPERS website at <http://www.calpers.ca.gov/eip-docs/about/pubs/employer/2012-st-body.pdf>.

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TABLE 28
PERF Schedule of Funding Progress
State Employees Only
(Fiscal Years Ended June 30)

(Dollars in Millions)

	<u>2002-03</u>	<u>2003-04</u>	<u>2004-05</u>	<u>2005-06</u>	<u>2006-07</u>	<u>2007-08</u>	<u>2008-09</u>	<u>2009-10</u>	<u>2010-11</u>	<u>2011-12</u>
Market Value of Assets (MVA)	\$56,843	\$65,488	\$74,050	\$81,968	\$96,988	\$91,349	\$68,179	\$76,266	\$91,159	\$88,810
Actuarial Value of Assets (AVA)	62,515	67,081	71,830	77,143	83,439	89,304	93,377	97,346	102,452	106,145
Actuarial Accrued Liabilities (AAL)-entry age	74,450	79,800	86,595	92,557	100,352	107,642	116,827	121,446	129,648	134,314
Excess of Market Value of Assets over AAL or Surplus (Unfunded) Actuarial Accrued Liabilities (UAAL) MVA Basis	(17,607)	(14,312)	(12,545)	(10,589)	(3,364)	(16,293)	(48,648)	(45,180)	(38,489)	(45,504)
Excess of Actuarial Value of Assets over AAL or Surplus (Unfunded) Actuarial Accrued Liabilities (UAAL) AVA Basis	(11,935)	(12,719)	(14,765)	(15,414)	(16,913)	(18,338)	(23,450)	(24,100)	(27,195)	(28,169)
Covered Payroll	12,628	12,624	12,935	13,299	14,571	15,890	16,333	16,281	16,212	15,680
Funded Ratio (MVA)	76.4 %	82.1 %	85.5 %	88.6%	96.6%	84.9%	58.4%	62.8%	70.3%	66.1%
Funded Ratio (AVA)	84.0%	84.1%	82.9%	83.3%	83.1%	83.0%	79.9%	80.2%	79.0%	79.0%

Source: CalPERS State and Schools Actuarial Valuation, Fiscal Year Ended June 30, 2012 and prior years.

State Contributions

As described above, required contributions to PERF are determined annually on an actuarial basis. Payments into PERF are made from the state and from employee contributions. State contributions are made from the General Fund, special funds, and non-governmental cost funds. From fiscal years 2007-08 to 2014-15, a range of approximately 55 to 63 percent of the state contributions to PERF are made from the General Fund. Table 29 shows the state's actual contributions to PERF for fiscal years 2007-08 through 2012-13 and estimated contributions for fiscal years 2013-14 and 2014-15. The state has made the full amount of actuarially required contribution each year.

TABLE 29
State Contribution to PERF, including CSU
Fiscal Years 2007-08 to 2014-15
Fiscal Year Ending June 30

(Dollars in Thousands)

<u>Fiscal Year</u>	<u>State Employees All Funds^(b)</u>	<u>State Employees General Fund^(b)</u>	<u>CSU Employees All Funds</u>	<u>CSU General Fund</u>	<u>Total Contributions</u>	<u>Total General Fund Contributions</u>
2007-08	\$2,999,455	\$1,649,700	N/A	N/A	\$2,999,455	\$1,649,700
2008-09	3,063,009	1,684,655	N/A	N/A	3,063,009	1,684,655
2009-10	2,860,787	1,573,433	N/A	N/A	2,860,787	1,573,433
2010-11	3,230,489	1,776,769	N/A	N/A	3,230,489	1,776,769
2011-12	3,174,494	1,745,972	N/A	N/A	3,174,494	1,745,972
2012-13	2,948,137	1,506,043	449,243	449,000	3,397,380	1,955,043 ^(b)
2013-14 ^(a)	3,219,262	1,644,546	473,798	473,542	3,693,060	2,118,088 ^(b)
2014-15 ^(a)	3,531,468	1,842,158	477,708	477,450	4,009,176	2,319,608 ^(b)

^(a) Estimated contributions.

^(b) Pension contributions for CSU employees are included for all years displayed in this table. However, beginning in 2012-13, CSU contributions are split out and identified separately.

Source: State of California, Department of Finance.

Prospective Funding Status; Future Contributions

The level of future required contributions from the state depends on a variety of factors, including future investment portfolio performance, actuarial assumptions, and additional potential changes in retirement benefits. There can be no assurances that the required annual contribution to CalPERS will not continue to significantly increase and that such increases will not materially adversely affect the financial condition of the state. See the caption "PENSION TRUSTS – General" for a discussion of new standards adopted by GASB. It is not known at this time how these changes in accounting and financial reporting will impact CalPERS' contribution policies.

The most recent valuation report for PERF contains a projection of future state contribution rates as a percentage of payroll under different investment return scenarios. The

tables that follow provide projected state contribution rates through fiscal year 2016-17 for each of the member categories under various scenarios. (CalPERS indicated that it intends to perform this analysis with each annual valuation.) The results below do not include the impact of the recent actuarial assumption changes adopted by the CalPERS Board on February 20, 2014. See “- Actuarial Assumptions.”

The estimated employer contribution rates displayed below are included in the 2014-15 Governor’s Budget.

	Fiscal Year 2014-15 Employer Contribution Rates
State Miscellaneous Tier 1	21.382%
State Miscellaneous Tier 2	21.726
State Industrial	16.764
State Safety	18.000
State Peace Officers & Firefighters	31.250
California Highway Patrol	36.419

In accordance with state law, the actuarial valuation for the fiscal year ended June 30, 2012 includes a sensitivity analysis of discount rates 2 percent lower and 2 percent higher than the current discount rate of 7.5 percent. The analysis displays potential required employer contribution rates assuming that the discount rate was adjusted to rates of 5.5 percent or 9.5 percent over the long term. The analysis shows that employer contribution rates are highly sensitive to changes in the discount rate and that employer contribution rates would be significantly reduced if a higher discount rate is used, and employer contribution rates would significantly increase if a lower discount rate is used. The actuarial report for the year ended June 30, 2012 contains information concerning the specific impact on employer contribution rates and unfunded liability resulting from these different discount rate assumptions.

The tables below show the projected state contribution rates for fiscal year 2015-16 through fiscal year 2017-18 for the employee categories under five different investment return scenarios. The contribution rates for fiscal year 2013-14 will not be affected by fiscal year 2012-13 investment returns. The contribution rates for 2016-17 and 2017-18 in the sensitivity analysis does not include the impact of the demographic assumption changes that were adopted by the CalPERS Board on February 20, 2014. The five different investment return scenarios were selected as follows (figures in parentheses are negative numbers):

The first scenario assumes a negative (4.10) percent return for each of the 2013-14, 2014-15 and 2015-16 fiscal years.

The second scenario assumes a 2.60 percent return for each of the 2013-14, 2014-15, and 2015-16 fiscal years.

The third scenario assumes the return for each of the 2013-14, 2014-15, and 2015-16 fiscal years would be CalPERS’ assumed 7.50 percent investment return.

The fourth scenario assumes an 11.90 percent return for each of the 2013-14, 2014-15, and 2015-16 fiscal years.

The fifth scenario assumes an 18.50 percent return for each of the 2013-14, 2014-15, and 2015-16 fiscal years.

<u>Estimated: 2015-16</u>					
Assumed return	(4.10)%	2.60%	7.50%	11.90%	18.50%
<u>Projected Contribution Rates</u>					
State Miscellaneous Tier 1	23.4%	22.8%	22.4%	22.0%	21.5%
State Miscellaneous Tier 2	23.3	22.7	22.3	22.0	21.4
State Industrial	17.0	16.6	16.3	16.0	15.7
State Safety	17.3	17.0	16.8	16.6	16.2
State Peace Officers & Firefighters	32.1	31.4	30.9	30.5	29.8
California Highway Patrol	37.8	37.1	36.6	36.1	35.4
Schools	13.4	12.9	12.6	12.3	11.9

Source: CalPERS State and Schools Actuarial Valuation, Fiscal Year Ended June 30, 2012.

<u>Estimated: 2016-17</u>					
Assumed return	(4.10)%	2.60%	7.50%	11.90%	18.50%
<u>Projected Contribution Rates</u>					
State Miscellaneous Tier 1	26.3%	24.7%	23.5%	22.4%	20.7%
State Miscellaneous Tier 2	26.3	24.8	23.6	22.5	20.8
State Industrial	18.9	17.8	16.9	16.1	14.9
State Safety	18.6	17.6	16.9	16.3	15.3
State Peace Officers & Firefighters	35.7	33.7	32.2	30.8	28.7
California Highway Patrol	41.6	39.6	38.1	36.7	36.7
Schools	15.8	14.5	13.6	12.7	11.3

Source: CalPERS State and Schools Actuarial Valuation, Fiscal Year Ended June 30, 2012.

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<u>Estimated: 2017-18</u>					
Assumed return	(4.10)%	2.60%	7.50%	11.90%	18.50%
<u>Projected Contribution Rates</u>					
State Miscellaneous Tier 1	29.9%	27.0%	24.7%	22.4%	18.8%
State Miscellaneous Tier 2	30.2	27.2	24.9	22.7	19.1
State Industrial	21.4	19.3	17.5	15.9	13.2
State Safety	20.3	18.5	17.1	15.8	13.6
State Peace Officers & Firefighters	40.3	36.5	33.5	30.7	26.1
California Highway Patrol	46.5	42.6	39.6	36.7	32.1
Schools	18.9	16.4	14.5	12.7	9.7

Source: CalPERS State and Schools Actuarial Valuation, Fiscal Year Ended June 30, 2012.

Investment Policy; Investment Returns

Pursuant to the state Constitution, the CalPERS Board has sole and exclusive fiduciary responsibility over the assets of the PERF. CalPERS' assets are managed both externally by professional investment management firms and internally by CalPERS investment staff. The CalPERS Board monitors the performance of the managers with the assistance of an external investment consultant.

CalPERS has established a series of procedures and guidelines with respect to investments. The procedures, grouped together as the "Investment Policy," serve to guide CalPERS' asset allocation strategy for PERF. The CalPERS Board reviews the Investment Policy annually, taking into consideration the latest actuarial valuation.

CalPERS follows a strategic asset allocation policy that identifies the percentage of funds to be invested in each asset class. Policy targets are typically implemented over a period of several years on market declines and through dollar cost averaging. Listed below is CalPERS' current asset allocation mix by market value and policy target percentages as of October 31, 2013. The strategic allocation policy may be changed by CalPERS from time to time. Additional information concerning CalPERS investments can be found on the CalPERS website.

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<u>Asset Class</u>	<u>Actual Investment (Billions)</u>	<u>Actual Investment</u>	<u>Interim Strategic Target ⁽¹⁾</u>
Growth – Public Equity	\$151.7	55.0%	47.0%
Growth – Private Equity	31.2	11.0	12.0
Income	41.0	15.0	19.0
Liquidity	10.6	4.0	2.0
Real Estate	23.7	9.0	11.0
Forestland/ Infrastructure	3.4	1.0	3.0
Inflation	9.4	3.0	6.0
Absolute Return Strategy	5.2	2.0	N/A
Multi Asset Class Strategy	<u>1.0</u>	<u>0.0</u>	<u>N/A</u>
Total Fund*	\$277.2	100.0%	100.0%

⁽¹⁾ Target allocation effective February 2013.

* Figures are rounded for viewing purposes.

Source: <http://www.calpers.ca.gov/index.jsp?bc=/investments/assets/assetallocation.xml>

The following tables set forth the total return on all assets for PERF for the fiscal years ending June 30, 2003 through June 30, 2013, as well as time-weighted average returns.

TABLE 30
CalPERS Investment Results Based On Market Value

<u>Fiscal Year</u>	<u>Annualized Rate of Return</u>
2002-03	3.7%
2003-04	16.6
2004-05	12.3
2005-06	11.8
2006-07	19.1
2007-08	(5.1)
2008-09	(24.0)
2009-10	13.3
2010-11	21.7
2011-12	0.1
2012-13	13.2

Source: CalPERS Comprehensive Annual Financial Report for Fiscal Years ended June 30, 2012 and June 30, 2013.

On January 13, 2014, a CalPERS press release reported a 16.2% return on investments for the calendar year ended December 31, 2013.

TABLE 31
PERF Time-Weighted Average Returns as of June 30, 2013

<u>Period</u>	<u>Time Weighted Average Rate of Return</u>
3 years	11.3%
5 years	3.5
10 years	7.1

Source: CalPERS Comprehensive Annual Financial Report for Fiscal Year ended June 30, 2012.

Investigation Affecting CalPERS

The previous use of placement agents by CalPERS' external investment managers has been the subject of investigations by various governmental authorities, including the U.S. Department of Justice, the U.S. Securities and Exchange Commission, and the California Attorney General's Office. Those law enforcement authorities have made extensive requests for documents and other information. According to CalPERS, it has cooperated and continues to cooperate with federal and state law enforcement authorities who are focused on whether civil or criminal laws have been violated by certain entities and individuals associated with CalPERS. In addition to its pending investigative efforts, the California Attorney General brought a civil action against a placement agent firm and other individuals in May 2010. That litigation is still pending.

In March 2011, CalPERS completed a special review of fees paid by its external managers to placement agents and their related activities. In connection with that review, CalPERS secured substantial fee reductions from a number of its external money managers and those managers agreed to no longer use placement agents for new CalPERS investments.

Other Retirement Plans

In addition to PERF, CalPERS also administers LRF, JRF, and JRF II, which are defined benefit plans.

In the JRF actuarial reports for the year ended June 30, 2012 CalPERS reported that, as of June 30, 2012, JRF had an unfunded actuarial liability of approximately \$3.1 billion and JRF II had an unfunded actuarial liability of approximately \$35.2 million. In the LRF actuarial report for the year ended June 30, 2012, CalPERS reported that LRF, as of June 30, 2012, had actuarial value of assets that exceeded the actuarial liability by approximately \$15.6 million. The state's fiscal year 2014-15 retirement contributions from the General Fund are estimated to be \$176.8 million for JRF, \$56.6 million for JRF II, and \$1.0 million for LRF.

Further information concerning JRF, JRF II, and LRF can be found in CalPERS' financial reports and actuarial reports and is set forth in Note 24 (and the Schedule of Funding Progress included in the Required Supplementary Information) to the Audited Basic Financial Statements of the State of California for the Year Ended June 30, 2012 attached as APPENDIX F to this Official Statement.

CalSTRS

General

CalSTRS was established under the California Education Code in 1913 to provide benefits to California public school and community college teachers and to certain other employees of the state's public school system (kindergarten through community college). CalSTRS is the administrator of multiple-employer, cost-sharing defined benefit plans, a tax-deferred defined contribution plan, a Medicare Premium Payment Program, and a Teachers' Deferred Compensation Fund.

The largest CalSTRS fund, the State Teachers' Retirement Plan (the "STRP"), is a multiple employer, cost-sharing, defined benefit plan comprised of four programs: the Defined Benefit Program (referred to in the state's 2012 Financial Statements and in this Official Statement as the "DB Program"), the Defined Benefit Supplement Program, the Cash Balance Benefit Program, and the Replacement Benefit Program. Within the DB Program there is also a Supplemental Benefits Maintenance Account (the "SBMA") which provides purchasing power protection for retired members.

The state is not an employer (with certain very limited exceptions) in any of CalSTRS programs but does contribute to the DB Program and the SBMA from its General Fund pursuant to statutes in the Education Code. The DB Program is funded through a combination of investment earnings and statutorily set contributions from three sources: the members of CalSTRS, the employers, and the state. Contribution rates for the members and employers to fund the DB Program are not adjusted to reflect or offset actual investment returns or other factors which affect the funded status of the DB Program. The same is true for the contribution rates for the state except that, if the funded status of the DB Program falls below a certain level, the state is required to make specified supplemental contributions to the DB Program.

As of June 30, 2012 (the fiscal year of the DB Program commences July 1 and ends June 30 of the following year), the DB Program's unfunded actuarial obligation was \$71.0 billion (67.0 percent funded ratio) based on an actuarial value of assets basis and \$80.4 billion (62.7 percent funded ratio) based on a market value of assets basis. The funding status triggered the requirement for the state to make specified supplemental contributions starting in the fiscal year ended June 30, 2012. See "Funding for the DB Program – State Contributions," "Funding Status," and "Prospective Funding Status; Future Contributions."

The funding of the DB Program was identified as a high-risk issue in the California State Auditor Report 2013 601 dated September 2013 because, as stated in the report, the DB Program assets are projected to be depleted in 31 years assuming existing contribution rates continue, and

other significant actuarial assumptions are realized. See “Prospective Funding Status; Future Contributions – Responsibility for the Unfunded Obligation.”

The SBMA is a separate account within the DB Program that is funded with a combination of investment earnings and statutorily set contributions from the state. The Purchasing Power Protection Program payments for retired members are made only to the extent funds are available in the SBMA and are not a vested benefit. See “Funding for the SBMA.”

CalSTRS is administered by a 12-member Teachers’ Retirement Board (the “CalSTRS Board”) that includes the California Director of Finance, State Controller, State Superintendent of Public Instruction, and the State Treasurer, who serve ex officio. The other CalSTRS Board members serve four-year terms and include three CalSTRS member-elected representatives representing current educators, one retired CalSTRS member, three public representatives, and one school board representative, each appointed by the Governor and confirmed by the Senate.

The CalSTRS Board appoints a Chief Executive Officer to administer CalSTRS and a Chief Investment Officer to direct investment of CalSTRS’ assets in accordance with CalSTRS Board policy. The CalSTRS Board also retains independent actuaries, auditors, and investment advisors. The CalSTRS Board has appointed Crowe Horwath LLP beginning with the fiscal year ended June 30, 2011 to serve as the independent auditor for CalSTRS, Pension Consulting Alliance to provide asset allocation and other investment analyses and Milliman, Inc. (the “CalSTRS Consulting Actuary”) to provide actuarial services to CalSTRS and for conducting specialized studies at the request of CalSTRS staff. The CalSTRS System Actuary, a CalSTRS employee, is responsible for reviewing the CalSTRS Consulting Actuary’s work for quality control purposes and also conducts day-to-day analyses as requested by CalSTRS staff.

Certain summary information concerning the DB Program is set forth below.

Members and Employers

As of June 30, 2013, the DB Program included 1,660 employers. The following table reflects the total number of members in the DB Program as of June 30, 2013 and 2012.

TABLE 32
DB Program Membership

<u>Membership</u>	<u>June 30, 2013</u>	<u>June 30, 2012</u>	<u>Percent Change</u>
Active Members	416,643	421,499	(1.2)
Inactive Members	182,576	178,655	2.2
Retirees and Beneficiaries	<u>269,274</u>	<u>262,038</u>	2.8
Total Membership	868,493	862,192	0.7

Source: CalSTRS Comprehensive Annual Financial Report for Fiscal Year ended June 30, 2013.

Retirement Benefits

Member benefits are determined by statute in the Education Code and are generally based on a member's age, final compensation, and years of credited service. Members are 100 percent vested in retirement benefits after five years of credited service and are eligible for normal retirement at age 60 and for early retirement at age 55 or at age 50 with 30 years of credited service. The normal retirement benefit is 2 percent of final compensation (as defined in the Education Code) for each year of credited service (up to 2.4 percent of final compensation for members retiring after age 60), and members who retired on or after January 1, 2001 with 30 or more years of service by December 31, 2010 receive monthly bonus payments of up to \$400 per month. Pension reform legislation signed in 2012 increased the retirement age for new CalSTRS members hired on or after January 1, 2013. New members who retire at age 62 will be eligible for a benefit equal to 2 percent of final compensation for each year of credited service (up to 2.4 percent of final compensation for members retiring after age 62).

Benefits are increased by 2 percent (a simple, not a compounded, cost-of-living increase) of the initial allowance, on each September 1 following the first anniversary of the effective date of the benefit.

The following table shows the amount of benefits and administrative expenses paid under the DB Program for the last seven fiscal years:

TABLE 33
DB Program
Schedule of Benefits Paid and Administrative Expenses

(Dollars in Millions)

<u>Fiscal Year</u>	<u>Amount of Benefits Paid</u>	<u>Administrative Expenses</u>
2006-07	\$ 7,168	\$106
2007-08	7,823	109
2008-09	8,604	113
2009-10	9,358	140
2010-11	10,092	110
2011-12	10,677	138
2012-13	11,355	137

Source: CalSTRS Comprehensive Annual Financial Reports for Fiscal Years ended June 30, 2007 through 2013.

Funding for the DB Program

The DB Program is funded with a combination of investment income and contributions from members, employers, and the state. Although specific amounts vary from year to year, approximately 55 percent of DB Program assets were derived from investment returns, according to CalSTRS. As described below, the contribution rates of the members, employers, and the state are determined by statute in the Education Code. There can be no assurances that the required amounts annually payable among the members, employers, and state will not significantly increase in the future.

Member Contributions. Members are required to make contributions to the DB Program in an amount equal to 8 percent of creditable compensation of the member. However, for services performed between January 1, 2000 and December 31, 2010, the member contribution to the DB Program was 6 percent because 2 percent was directed to the Defined Benefit Supplement Program (to which the state does not contribute).

Employer Contributions. Employers are required to make contributions to the DB Program in an amount equal to 8 percent of creditable compensation plus 0.25 percent to pay costs of the unused sick leave credit; provided that a portion of the employers' contributions has in the past and may in the future be transferred to the Medicare Premium Program which has the effect of further reducing aggregate annual contributions to the DB Program.

State Contributions. The state's General Fund contribution to the DB Program is 2.017 percent of creditable compensation from two fiscal years prior. For example, for fiscal year 2011-12, the state's contribution was based on creditable compensation from fiscal year 2009-10. The state also contributes an additional 0.524 percent of creditable compensation from two fiscal years prior when there is an unfunded obligation or a normal cost deficit exists for benefits in place as of July 1, 1990. The percentage is adjusted up to 0.25 percent per year to reflect the contributions required to fund the unfunded obligation or the normal cost deficit. However, the supplemental contribution may not exceed 1.505 percent of creditable compensation from two fiscal years prior.

Based on the most recent actuarial valuation, as of June 30, 2012, an unfunded obligation exists for the benefits in place as of July 1, 1990, which triggered the supplemental payments for the fiscal year ending June 30, 2012 at a contribution rate of 0.524 percent starting October 1, 2011. An appropriation for this supplemental contribution was included in the 2011 Budget Act. An increased supplemental contribution rate to 0.774 percent was included in the 2012 Budget Act and 1.024 percent is included in the 2013 Budget Act.

The 2014-15 Governor's Budget assumes that the supplemental contribution rate will increase to 1.274 percent. The following table displays the annual actuarially required contributions, the actual contributions for employers, and the percentage of the actuarially required contribution that has been funded by the employers and the state for the last six fiscal years. Contributions from the state are displayed for the budget year and the previous seven fiscal years.

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TABLE 34
DB Program
Schedule of Contributions from Employers and the State
(Dollars in Millions)

Fiscal Year	Annual Actuarially Required Contribution^(a)	Contributed by Employers^(b)	Contributed by State^(c)	Total Contributed	Percent of Actuarially Required Contribution Contributed
2007-08	\$4,362	\$2,363	\$501	\$2,864	66%
2008-09	4,547	2,331	536	2,867	63
2009-10	4,924	2,130	563	2,693	55
2010-11	5,985	2,228	568	2,796	47
2011-12	6,230	2,166	653	2,819	45
2012-13	6,629	2,192	718	2,910	44
2013-14	Not yet released	Not yet released	779	Not yet released	Not yet released
2014-15	Not yet released	Not yet released	843	Not yet released	Not yet released

(a) For the DB Program Annual Required Contribution for employers and state, an open amortization period of 30 years is used by the CalSTRS Consulting Actuary to determine the unfunded actuarial liability.

(b) For employer contributions, amounts are reduced by the amount of transfers to the Medicare Premium Program.

(c) State of California, Department of Finance; fiscal years ending June 30, 2014 and 2015 are estimated; amount contributed by state in fiscal year 2007-08 differs from amount reflected in CalSTRS Comprehensive Annual Financial Report for Fiscal Year ended June 30, 2012 due to timing issues. The fiscal years ending June 30, 2012, 2013, 2014, and 2015 include the pre-1990 benefit described on the previous page. For 2012, the 0.524 percent contribution equates to \$106.5 million, for 2013, the 0.774 percent contribution equates to \$188.0 million, for 2014, the 1.024 percent contribution equates to \$251.5 million and for 2015, the 1.274 percent contribution equates to \$316.4 million.

Source: CalSTRS Comprehensive Annual Financial Report for Fiscal Year ended June 30, 2013 (except as noted in footnote (c) to this Table 34).

Actuarial Methods and Assumptions

Although contributions are set by statute, the CalSTRS Consulting Actuary prepares annual actuarial valuation reports of the DB Program. The CalSTRS Consulting Actuary also prepares reports reviewing the DB Program's actual experience every four years. The CalSTRS Board uses experience reports to evaluate how realistic the long-term assumptions have been and may be in the future. The most recent valuation report for the DB Program, dated March 26, 2013 (the "2012 CalSTRS Valuation"), was prepared as of June 30, 2012, and is available on the CalSTRS website. The actuarial assumptions and methods used in the 2012 CalSTRS Valuation were based on the most recent experience report (the "2010 Experience Analysis") prepared by the CalSTRS Consulting Actuary in February 2012.

In preparing the 2012 CalSTRS Valuation, the CalSTRS Consulting Actuary used the Entry Age Actuarial Cost Method to measure the accruing costs of benefits under the DB Program. GASB Statement 68 will require all state and local governments with pension

liabilities to use the Entry Age Actuarial Cost Method beginning in fiscal year 2014-15 if they are not already doing so. Under the Entry Age Actuarial Cost Method, the actuarial present value of projected benefits of each individual is allocated on a level basis over the earnings of the individual between entry age and assumed exit age. The portion of the actuarial present value allocated to the valuation year is called the normal cost and represents the cost assigned to a member for a given year, such that it would meet the continuing costs of a particular benefit if contributed each year starting with the date of membership. The CalSTRS Consulting Actuary notes that the Entry Age Actuarial Cost Method is designed to produce a normal cost rate that remains a level percentage of earned salaries and that the normal cost rate is expected to remain fairly stable so long as the benefit provisions are not amended, the assumptions are not changed, membership experience emerges as assumed, and the demographic characteristics of the membership remain reasonably consistent. Some of the key demographic information taken into account includes assumptions about membership, service retirements, disability retirements, deaths, and merit salary increases, and some of the economic items include assumptions about inflation and wage growth.

The portion of the actuarial value of benefits not provided for at a valuation date by the actuarial present value of future normal costs is called the actuarial obligation, and the excess, if any, of the actuarial obligation over the actuarial value of assets is the unfunded actuarial obligation. Assumptions about how long benefits will be paid for active and inactive members and when such members will retire and how long they will live are required in calculating the actuarial obligation, and economic assumptions and valuation methods are required in valuing assets. The following table sets forth certain actuarial methods and assumptions for the four fiscal years ended June 30, 2013.

On June 25, 2012, GASB adopted Statement 67, which is effective beginning in fiscal year 2013-14. See the caption, "PENSION TRUSTS – General." GASB Statement 67 will change the rate used to discount projected benefit payments to their present value (the "Discount Rate") for underfunded pension plans under specific conditions. GASB has stated that GASB Statement 67 will require the Discount Rate for some insufficiently funded plans to be based on a single rate that reflects a blend of the actuarially assumed investment return and the yield or index rate on tax-exempt 20-year AA/Aa-or-higher rated general obligation municipal bonds. There can be no assurance that such change will not apply to the DB Program. The final text of GASB Statement 67 was released on August 2, 2012, and the full effect on the new standards on CalSTRS financial statements is not known at this time. CalSTRS staff has indicated on a preliminary basis that the application of a lower Discount Rate would increase the reported unfunded liability for the DB Program.

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TABLE 35
Certain Actuarial Methods and Assumptions Utilized For DB Program
Fiscal Year Ending June 30

	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>
Methods				
Actuarial Cost Method	Entry age normal	Entry age normal	Entry age normal	Entry age normal
Amortization Method	Level Percent of payroll	Level Percent of payroll	Level Percent of payroll	Level Percent of payroll
Amortization Period	Open	Open	Open	Open
Remaining Amortization Period	30 years	30 years	30 years	30 years
Asset Valuation Method	Expected value with 33% adjustment to market value	Expected value with 33% adjustment to market value	Expected value with 33% adjustment to market value	Expected value with 33% adjustment to market value
Actuarial Assumptions				
Investment Rate of Return	7.75%	7.50%	7.50%	7.50%
Interest on Accounts	6.00	4.50	4.50	4.50
Wage Growth	4.00	3.75	3.75	3.75
Consumer Price Inflation	3.00	3.00	3.00	3.00
Post-retirement Benefit Increases	2.00 (simple)	2.00 (simple)	2.00 (simple)	2.00 (simple)

Source: CalSTRS Comprehensive Annual Financial Reports for Fiscal Years ended June 30, 2010, 2011, 2012, and 2013.

Actuarial Valuation

According to CalSTRS and as reflected in the 2012 CalSTRS Valuation, the biggest source of funding of the DB Program is investment returns, and in calculating the actuarial value of assets, contributions for the past year are added to the actuarial value of assets at the end of the prior year; benefits and expenses are subtracted; an assumed rate of return is added, and as described below, a portion of market value gains and losses are added or subtracted. The assumed investment rate of return on DB Program assets (net of investment and administrative expenses) and the assumed interest to be paid on refunds of member accounts are based in part on an inflation assumption of 3.0 percent.

See the caption “Actuarial Methods and Assumptions” above for a discussion of expected changes in GASB standards that could change the Discount Rate used to calculate the DB Program’s unfunded actuarial obligation from a long-term assumed investment rate of return to a blend of the long term assumed investment rate of return and a yield or index rate.

Actual market returns are taken into account but to reduce rate volatility, actual market gains and losses are spread or “smoothed” over a three-year period. That is, one third of the difference between the expected actuarial value of assets and the fair market value of assets is taken into account to determine the actuarial value of assets. According to the 2012 CalSTRS Valuation, due to the asset smoothing method, approximately one-third of the approximately \$3.89 billion investment loss was recognized in June 30, 2012 (the difference between the AVA and MVA in Table 36 below). As discussed under the caption “PENSION TRUSTS – General,” GASB Statements 67 and 68, beginning in fiscal year 2013-14 for pension plans and fiscal year

2014-15 for employers, will require state and local governments with pension liabilities to recognize the differences between expected and actual investment returns over a closed 5 year period instead of the 3-year period currently used by CalSTRS. It is not known at this time how this change will impact the DB Program.

Funding Status

The following table sets forth the schedule of funding progress as of the ten most recent actuarial valuation dates based on information provided by CalSTRS from the actuarial valuation reports for such years. Funding progress is measured by a comparison of DB Program assets with DB Program liabilities.

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TABLE 36
DB Program Schedule of Funding Progress
(Fiscal Years Ended June 30)

(Dollars in Millions)

	<u>2002-03</u>	<u>2003-04</u>	<u>2004-05</u>	<u>2005-06</u>	<u>2006-07</u>	<u>2007-08</u>	<u>2008-09</u>	<u>2009-10</u>	<u>2010-11</u>	<u>2011-12</u>
Market Value of Assets (MVA) ^(a)	NA	NA	NA	NA	NA	NA	NA	\$117,129	\$140,040	\$134,835
Actuarial Value of Assets (AVA)	\$108,667	\$114,094	\$121,882	\$131,237	\$146,419	\$155,215	\$145,142	140,291	143,930	144,232
Actuarial Accrued Liabilities (AAL)-entry age	131,777	138,254	142,193	150,872	167,129	177,734	185,683	196,315	208,405	215,189
Excess of Market Value of Assets over AAL or Surplus (Unfunded) Actuarial Accrued Liabilities (UAAL) MVA Basis ^(a)	NA	NA	NA	NA	NA	NA	NA	(79,186)	(68,365)	\$(80,354)
Excess of Actuarial Value of Assets over AAL or Surplus (Unfunded) Actuarial Accrued Liabilities (UAAL) AVA Basis	(23,110)	(24,160)	(20,311)	(19,635)	(20,710)	(22,519)	(40,541)	(56,024)	(64,475)	(70,957)
Covered Payroll	23,867	22,589	23,257	24,240	25,906	27,118	27,327	26,275	25,576	25,388
Funded Ratio (MVA) ^(a)	NA	NA	NA	NA	NA	NA	NA	60%	67%	63%
Funded Ratio (AVA)	82%	83%	86%	87%	88%	87%	78%	71%	69%	67%

^(a) The CalSTRS Comprehensive Annual Financial Report reports the SBMA assets with DB Program assets and does not provide a separate accounting of only the DB Program assets. Therefore, market values for DB Program assets were not available for the fiscal years ended June 30, 2003 to 2009. The market value of the DB Program assets (without SBMA assets) for the fiscal year ended June 30, 2010, June 30, 2011 and June 30, 2012 was provided by the CalSTRS Consulting Actuary.

Source: CalSTRS Actuarial Valuations for Fiscal Years ended June 30, 2003 through 2012.

According to the CalSTRS Comprehensive Annual Financial Report for Fiscal Year ended June 30, 2012, the market value of the entire DB Program investment portfolio (including the SBMA assets) was \$150.6 billion, a decrease from \$155.5 billion or -3.2 percent over June 30, 2011.

Prospective Funding Status; Future Contributions

In the 2012 CalSTRS Valuation, the CalSTRS Consulting Actuary concluded that the unfunded actuarial obligation will not be amortized over any future period and that the DB Program is projected to have its assets depleted in about 31 years. This was primarily due to lower investment return experience since 2000. The CalSTRS Consulting Actuary also determined in the CalSTRS Valuation for June 30, 2010 that a supplemental contribution of 0.524 percent of creditable compensation was required to be paid by the state beginning in the fiscal year ended June 30, 2012 (commencing with the first quarterly payment due October 1, 2011) because as of June 30, 2010 there was an unfunded actuarial obligation related to the 1990 structure discussed above under “Funding for the DB Program – State Contributions.” The 2011 Budget Act included an appropriation related to this statutorily required supplemental contribution. In the CalSTRS Valuation for June 30, 2011, the CalSTRS Consulting Actuary determined that an increase of 0.25 percent in the supplemental contribution, for a total supplemental contribution of 0.774 percent would be required for fiscal year 2012-13. The increased supplemental contribution rate of 0.774 percent was included in the 2012 Budget Act. In the 2012 CalSTRS Valuation, the CalSTRS Consulting Actuary determined that an increase of 0.25 percent in the supplemental contribution, for a total supplemental contribution of 1.024 percent, will be required for fiscal year 2013-14. The increased supplemental contribution rate of 1.024 percent is included in the 2013 Budget Act.

Using the CalSTRS Board’s methods and assumptions as of June 30, 2012, the CalSTRS Consulting Actuary calculated that to amortize the unfunded actuarial obligation as of June 30, 2012 over 30 years, a level combined contribution rate of 34.092 percent (an increase to existing combined contribution rates of 14.620 percent and assuming the state’s supplemental contribution is adjusted as required by current statutes), beginning on July 1, 2012, would be required. This is an increase of 1.695 percentage points from what the valuation for June 30, 2011 indicated was necessary. These figures do not incorporate the impact of the 13.8 percent investment return earned by the system in 2012-13. See “PENSION TRUSTS – Pension Reform.”

See the caption “Actuarial Methods and Assumptions” above for a discussion of expected changes in GASB standards that could change the Discount Rate used to calculate the DB Program’s unfunded actuarial obligation from a long-term assumed investment rate of return to a blend of the long term assumed investment rate of return and a yield or index rate.

The following table sets forth the amortization of the unfunded actuarial obligation of the DB Program assuming that the contribution rates and actuarial assumptions as of June 30, 2012 continue to be utilized. The table shows the amount available to amortize the unfunded actuarial obligation after payment of the normal cost on a year-by-year basis and the unfunded actuarial obligation growing from \$79.4 billion in 2012 to \$616.8 billion in 2042.

TABLE 37
DB Program
Amortization of Unfunded Actuarial Obligation^{(a)(b)}

(Dollars in Millions)

<u>Year</u>	<u>Fiscal Year</u>	<u>Beginning Unfunded Act. Oblig.</u>	<u>Amortization Payment</u>			<u>Interest Charge at 7.50%</u>	<u>Recognition of Deferred Asset Losses</u>	<u>Ending Unfunded Act. Oblig.</u>
			<u>Total Contrib.</u>	<u>Normal Cost</u>	<u>Available Amtzn.</u>			
1	2012-13	\$70,957	\$5,093	\$4,874	\$219	\$5,314	\$3,367	\$79,419
2	2013-14	79,419	5,304	5,036	268	5,947	2,413	87,511
3	2014-15	87,511	5,541	5,204	337	6,551	1,729	95,454
4	2015-16	95,454	5,811	5,377	434	7,143	1,239	103,402
5	2016-17	103,402	6,028	5,557	471	7,738	888	111,557
6	2017-18	111,557	6,252	5,742	510	8,348	637	120,032
7	2018-19	120,032	6,485	5,933	552	8,982	456	128,918
8	2019-20	128,918	6,727	6,131	596	9,647	327	138,296
9	2020-21	138,296	6,978	6,334	644	10,349	234	148,235
10	2021-22	148,235	7,238	6,544	694	11,902	168	158,801
11	2022-23	158,801	7,507	6,761	746	11,883	120	170,058
12	2023-24	170,058	7,787	6,984	803	12,725	86	182,066
13	2024-25	182,066	8,077	7,214	863	13,623	62	194,888
14	2025-26	194,888	8,378	7,451	927	14,583	44	208,588
15	2026-27	208,588	8,690	7,696	994	15,608	32	223,234
16	2027-28	223,234	9,014	7,948	1,066	16,703	23	238,894
17	2028-29	238,894	9,350	8,206	1,144	17,875	16	255,641
18	2029-30	255,641	9,698	8,472	1,226	19,128	12	273,555
19	2030-31	273,555	10,059	8,744	1,315	20,468	8	292,716
20	2031-32	292,716	10,433	9,024	1,409	21,902	6	313,215
21	2032-33	313,215	10,821	9,312	1,509	23,436	4	335,146
22	2033-34	335,146	11,224	9,610	1,614	25,077	3	358,612
23	2034-35	358,612	11,642	9,918	1,724	26,833	2	383,723
24	2035-36	383,723	12,075	10,238	1,837	28,712	2	410,600
25	2036-37	410,600	12,525	10,569	1,956	30,723	1	439,368
26	2037-38	439,368	12,991	10,913	2,078	32,876	1	470,167
27	2038-39	470,167	13,475	11,207	2,205	35,181	1	503,144
28	2039-40	503,144	13,978	11,643	2,335	37,650	0	538,459
29	2040-41	538,459	14,499	12,031	2,468	40,294	0	576,285
30	2041-42	576,285	15,040	12,437	2,603	43,126	0	616,808

^(a) Based on the actuarial value of assets with projected recognition of deferred known asset losses as of June 30, 2012.

^(b) Supplemental State contributions under Education Code §22955(b) are included, as they are required based on the current valuation.

Source: CalSTRS Actuarial Valuations for Fiscal Year ended June 30, 2012.

Responsibility for the Unfunded Obligation

As explained above, total statutorily required contributions, when added to investment earnings, have been significantly less than the actuarially required contributions necessary to fully fund the DB Program on an actuarial basis. The CalSTRS Consulting Actuary noted in the 2012 CalSTRS Valuation Report that the DB Program assets would be depleted in about

31 years assuming existing contribution rates continue, and other significant actuarial assumptions are realized. Other than the state's requirement to contribute specified supplemental contributions under certain conditions described above, the state is not required under existing statutes to increase its contributions (only the Legislature can change the statutes requiring the state's contribution), and the Administration does not believe that the state is otherwise required to provide funding for the outstanding liability.

CalSTRS has stated on a number of occasions, including in a letter from the Chief Executive Officer of CalSTRS contained within the CalSTRS Comprehensive Annual Financial Report for the Fiscal Year ended June 30, 2010, that it believes based on its analysis of case law and statutes that the state is responsible for providing an actuarially sound retirement system and paying the difference between the benefits paid and the contributions received in the event that the DB Program assets are depleted. Subsequently, in the Comprehensive Annual Financial Report for the Fiscal Year ended June 30, 2011, the Chief Executive Officer of CalSTRS stated the Legislature and the Governor must craft a specific funding strategy involving increased contributions, which can be "gradual, predictable, and fair to all parties." The Administration does not agree with CalSTRS' position regarding the state's responsibility. The Administration believes that there are a number of ways to address the unfunded liability, including increased employer and employee contributions and other reforms.

In accordance with state law, the Bureau of State Audits periodically identifies what it believes to be "high risk" issues facing the state. The funding of the DB Program was identified as a new high-risk issue in the California State Auditor Report 2011-601 dated August 2011. In its most recent report 2013-601 on state "High Risk" issues, dated September 2013, the Bureau continued to include funding of the DB Program in this category. Excerpts from this portion of the 2013 report are set out below:

"To limit the risk of not having enough assets to cover retirement benefits, the U.S. Government Accountability Office recommends that retirement systems maintain a funding ratio of at least 80 percent of liabilities.... However, poor investment returns due to the economic recession, as well as the inability to adjust contributions, have caused the funding ratio of the CalSTRS Defined Benefit Program to decrease from 98 percent in 2001 to 67 percent in 2012....

One of the major risks to CalSTRS' funding is that its board does not have the authority to set contribution rates.... [O]nly the Legislature, not the CalSTRS board, has the authority to change the contribution rates. ... The member and employer contribution rates have remained largely unchanged by the Legislature since 1972 and 1990, respectively....

At the current contribution rate and actuarially estimated rate or return on investment, the Defined Benefit Program's funding ratio will continue to drop and assets will eventually be depleted....

As time passes, it will be harder to reverse the downward trend, and the required increase in contributions may grow too large for the State to take necessary action. According to a March 2013 actuarial valuation report, even assuming the expected return on CalSTRS'

investments is achieved each year, the Defined Benefit Program is at risk of having its funding status continue to decrease to zero in 31 years if the Legislature does not increase contribution rates. Because the State may bear some responsibility for funding the benefits promised to CalSTRS members, unless the State takes steps to ensure that funding for the CalSTRS program is increased, it may have to make up for the deficit using revenue from taxes. Consequently, this remains a high-risk issue for the State....”

No assurance can be given that the state’s contributions to the DB Program will not be increased substantially in the future.

On February 14, 2013, CalSTRS submitted a report to the Legislature on the funding of the DB Program in response to SCR 105. See “Pension Reform” above.

Investment Policy; Investment Returns

Pursuant to the state Constitution, the CalSTRS Board has sole and exclusive fiduciary responsibility over all CalSTRS’ assets (including the DB Program assets). CalSTRS’ assets (including the DB Program assets) are managed both externally by professional investment management firms and internally by CalSTRS investment staff. The CalSTRS Board monitors the performance of the managers with the assistance of an external investment consultant. See “General” above.

CalSTRS has established a series of procedures and guidelines with respect to investments. The procedures, grouped together as the “Investment Policy and Management Plan,” serve to guide CalSTRS asset allocation strategy for all CalSTRS’ programs, including the DB Program. The CalSTRS Board reviews the Investment Policy and Management Plan annually, taking into consideration the latest actuarial study. CalSTRS follows strategic allocation guidelines that identify targets for the percentage of funds to be invested in each asset class. These targets are typically implemented over a period of several years. Listed below is CalSTRS current asset allocation mix by market value and guideline target percentages. The strategic allocation guidelines may be changed by the CalSTRS Board from time to time. Additional information concerning CalSTRS investments can be found on the CalSTRS website.

<u>Asset</u>	<u>Market Value (Millions)⁽¹⁾</u>	<u>Actual %⁽¹⁾</u>	<u>Current Target %⁽²⁾</u>
Global Equity	\$ 100,421	56.9%	55.0%
Fixed Income	28,139	16.0	17.0
Real Estate	21,498	12.2	13.0
Private Equity	21,209	12.0	13.0
Cash	2,899	1.6	1.0
Inflation Sensitive	919	0.5	1.0
Absolute Return	<u>1,327</u>	<u>0.8</u>	<u>0.0</u>
Total Investment Assets	\$176,412	100.0%	100.0%

⁽¹⁾ As of November 30, 2013.

⁽²⁾ Target Allocation adopted September 10, 2013.

Source: <http://www.calstrs.com/current-investment-portfolio>

The following table sets forth the total return on all CalSTRS' assets (including the DB Program assets) for the fiscal years ended June 30, 2003 through June 30, 2013, as well as time-weighted average returns.

TABLE 38
CalSTRS Investment Results Based On Market Value

<u>Fiscal Year</u>	<u>Annualized Rate of Return</u>
2002-03	3.41%
2003-04	17.38
2004-05	11.09
2005-06	13.21
2006-07	21.03
2007-08	(3.69)
2008-09	(25.03)
2009-10	12.20
2010-11	23.10
2011-12	1.84
2012-13	13.80

Source: CalSTRS Comprehensive Annual Financial Report for Fiscal Year ended June 30, 2013.

TABLE 39
CalSTRS Time-Weighted Average Returns as of June 30, 2013

<u>Period</u>	<u>Time- Weighted Rate of Return</u>
3 years	12.57%
5 years	3.72
10 years	7.53

Source: CalSTRS Comprehensive Annual Financial Report for Fiscal Year ended June 30, 2013.

Funding for the SBMA

The SBMA is a separate account within the DB Program that is funded with a combination of investment income and contributions from the state. The contribution rate for the state's funding of the SBMA is also determined by statute in the Education Code. The Purchasing Power Protection Program funded from the SBMA provides quarterly payments to retired and disabled members and beneficiaries to restore purchasing power to beneficiaries if the purchasing power of their initial retirement or disability allowances have fallen below a specified percentage. The Purchasing Power Protection Program payments are made only to the extent funds are available in the SBMA and are not a vested benefit.

State Contributions. The state's General Fund contribution to the SBMA is 2.5 percent of creditable compensation of the fiscal year ending in the prior calendar year, less \$70 million for the fiscal year ended June 30, 2010, \$71 million for the fiscal year ended June 30, 2011 and \$72 million thereafter. The following table summarizes funding of the SBMA during the nine fiscal years ending June 30, 2015. The Education Code requires the state to continue contributions to the SBMA and that the unused balances remain in the SBMA even if they exceed the amounts required to be paid to beneficiaries.

TABLE 40
SBMA Funding

<u>Fiscal Year</u>	<u>General Fund Contributions</u> ⁽¹⁾	<u>Benefit Payments</u>	<u>Interest</u>	<u>Reserve</u>
2006-07	\$ 598,390,798	\$224,130,894	\$224,218,226	\$3,399,499,340
2007-08	1,121,500,844 ⁽²⁾	223,337,493	271,959,947	4,569,622,638
2008-09	597,474,363 ⁽³⁾	341,069,179	365,569,811	5,302,830,510
2009-10	684,935,046	266,244,852	424,226,441	6,112,989,062
2010-11	689,633,129	245,823,604	489,039,125	6,988,857,762
2011-12	662,743,780	234,612,293	554,436,996	8,283,302,000
2012-13	641,762,636	221,451,000	Not yet released	9,269,803,000
2013-14 ⁽⁴⁾	581,260,411	Not yet released	Not yet released	Not yet released
2014-15 ⁽⁴⁾	580,819,474	Not yet released	Not yet released	Not yet released

⁽¹⁾ State of California, Department of Finance; fiscal years ending June 30, 2014 and 2015 are estimated.

⁽²⁾ In the fiscal year ended June 30, 2004, the Legislature reduced the planned \$558,867,986 contribution by \$500 million. After litigation, the state was ordered to repay the \$500 million with interest. The principal amount was repaid in the fiscal year ended June 30, 2008, and the interest is to be paid in four annual installments beginning with the fiscal year ended June 30, 2010. The interest payments are included in the contribution amounts for the respective years.

⁽³⁾ The Education Code was amended to reduce the amount transferred from the General Fund and to provide that the transfer be made in two equal payments, one on November 1 and the second on April 1.

⁽⁴⁾ Estimated.

Source: CalSTRS Comprehensive Annual Financial Report for Fiscal Year ended June 30, 2013 and a 2011 Report to the Governor and the Legislature (except as noted in footnote 1 to this Table 40).

THE BUDGET PROCESS

General

The state's fiscal year begins on July 1 and ends on June 30 of the following year. The state's General Fund budget operates on a legal basis, generally using a modified accrual system of accounting for its General Fund, with revenues credited in the period in which they are measurable and available and expenditures debited in the period in which the corresponding liabilities are incurred.

The annual budget is proposed by the Governor by January 10 of each year for the next fiscal year (the "Governor's Budget"). Under state law and the state constitution, the annual proposed Governor's Budget cannot provide for projected expenditures in excess of projected resources for the ensuing fiscal year. Following the submission of the Governor's Budget, the

Legislature takes up the proposal. As required by the Balanced Budget Amendment (“Proposition 58”) and as described below, beginning with fiscal year 2004-05, the Legislature may not pass a budget bill in which General Fund expenditures exceed estimated General Fund revenues and beginning fund balances at the time of the passage and as set forth in the budget bill.

Under the state Constitution, money may be drawn from the State Treasury only through an appropriation made by law. The primary source of annual expenditure appropriations is the annual Budget Act as approved by the Legislature and signed by the Governor. Pursuant to Proposition 25, enacted on November 2, 2010, the Budget Act (or other appropriation bills and “trailer bills” which are part of a budget package) must be approved by a majority vote of each House of the Legislature. (This was a reduction from a requirement for a two-thirds vote.) The Governor may reduce or eliminate specific line items in the Budget Act or any other appropriations bill without vetoing the entire bill. Such individual line-item vetoes are subject to override by a two-thirds majority vote of each House of the Legislature.

Appropriations also may be included in legislation other than the Budget Act. Continuing appropriations, available without regard to fiscal year, may also be provided by statute or the state Constitution.

Funds necessary to meet an appropriation are not required to be in the State Treasury at the time an appropriation is enacted; revenues may be appropriated in anticipation of their receipt.

Constraints on the Budget Process

Over the years, a number of laws and constitutional amendments have been enacted, often through voter initiatives, which have made it more difficult for the state to raise taxes, restricted the use of the state’s General Fund or special fund revenues, or otherwise limited the Legislature and the Governor’s discretion in enacting budgets. Historic examples of provisions that make it more difficult to raise taxes include Proposition 13, passed in 1978, which, among other things, required that any change in state taxes enacted for the purpose of increasing revenues collected pursuant thereto, whether by increased rates or changes in computation, be approved by a two-thirds vote in each house of the Legislature, and Proposition 4, approved in 1979, which limits government spending by establishing an annual limit on the appropriation of tax proceeds. Examples of provisions restricting the use of General Fund revenues are Proposition 98, passed in 1988, which mandates that a minimum amount of General Fund revenues be spent on local education, and Proposition 10, passed in 1998, which raised taxes on tobacco products and mandated how the additional revenues would be expended. See “STATE FINANCES – Proposition 98 and K-14 Funding” and “- Sources of Tax Revenue – Taxes on Tobacco Products.”

Constitutional amendments approved by the voters have also affected the budget process. These include Proposition 49, approved in 2002, which requires the expansion of funding for before and after school programs. Proposition 58, approved in 2004, which requires the adoption of a balanced budget and restricts future borrowing to cover budget deficits; Proposition 63, approved in 2004, which imposes a surcharge on taxable income of more than \$1 million and

earmarks this funding for expanded mental health services; Proposition 1A, approved in 2004, which limits the Legislature's power over local revenue sources, and Proposition 1A, approved in 2006, which limits the Legislature's ability to use sales taxes on motor vehicle fuels for any purpose other than transportation. Propositions 22 and 26, approved on November 2, 2010, further limit the state's fiscal flexibility. Proposition 25, also passed by the voters in November 2010, changed the legislative vote requirement to pass a budget and budget related legislation from two-thirds to a simple majority. It retained the two-thirds vote requirement for taxes. Proposition 30, approved on November 6, 2012, among other things, placed into the state Constitution the current statutory provisions transferring 1.0625 percent of the state sales tax to local governments to fund realignment; and Proposition 39, also approved on November 6, 2012, among other things, dedicates for five years up to \$550 million annually to clean energy projects out of an expected \$1 billion annual increase in corporate tax revenue due to reversal of a provision adopted in 2009 that gave corporations an option on how to calculate their state income tax liability.

These approved constitutional amendments are described below.

Balanced Budget Amendment (Proposition 58)

Proposition 58, approved by the voters in 2004, requires the state to enact a balanced budget, and establish a special reserve, and restricts certain future borrowing to cover fiscal year end deficits. As a result of the provisions requiring the enactment of a balanced budget and restricting borrowing, the state would in some cases have to take more immediate actions to correct budgetary shortfalls. Beginning with the budget for fiscal year 2004-05, Proposition 58 requires the Legislature to pass a balanced budget and provides for mid-year adjustments in the event that the budget falls out of balance and the Governor calls a special legislative session to address the shortfall. The balanced budget determination is made by subtracting estimated expenditures from all resources expected to be available, including prior-year balances.

If the Governor determines that the state is facing substantial revenue shortfalls or spending increases, the Governor is authorized to declare a fiscal emergency. He or she would then be required to propose legislation to address the emergency, and call the Legislature into special session for that purpose. If the Legislature fails to pass and send to the Governor legislation to address the fiscal emergency within 45 days, the Legislature would be prohibited from: (i) acting on any other bills or (ii) adjourning in joint recess until such legislation is passed.

Proposition 58 also required the establishment of the Budget Stabilization Account, which is funded by annual transfers of specified amounts from the General Fund, unless suspended or reduced by the Governor or until a specified maximum amount has been deposited.

Proposition 58 also prohibits the use of general obligation bonds, revenue bonds, and certain other forms of borrowing to cover fiscal year end budget deficits. The restriction does not apply to certain other types of borrowing, such as: (i) short-term borrowing to cover cash shortfalls in the General Fund (including revenue anticipation notes or revenue anticipation warrants currently used by the state), or (ii) inter-fund borrowings.

Local Government Finance (Proposition 1A of 2004)

As described under “STATE FINANCES – Local Governments,” Senate Constitutional Amendment No. 4 (also known as “Proposition 1A of 2004”), approved by the voters in the November 2004 election, amended the state Constitution to, among other things, reduce the Legislature’s authority over local government revenue sources by placing restrictions on the state’s access to local governments’ property, sales, and vehicle license fee revenues as of November 3, 2004. Beginning with fiscal year 2008-09, the state was able to borrow up to 8 percent of local property tax revenues, but only if the Governor proclaimed such action was necessary due to a severe state fiscal hardship and two-thirds of both houses of the Legislature approve the borrowing. The amount borrowed is required to be paid back within three years. In addition, the state cannot reduce the local sales tax rate or restrict the authority of local governments to impose or change the distribution of the statewide local sales tax.

The provisions of Proposition 1A of 2004 allowing the state to borrow money from local governments from time to time have been repealed by Proposition 22 of 2010, which permanently prohibits any future such borrowing. However, prior to such repeal, the Amended 2009 Budget Act authorized the state to exercise its Proposition 1A of 2004 borrowing authority. This borrowing generated \$1.998 billion that was used to offset state General Fund costs for a variety of court, health, corrections, and K-12 programs. Pursuant to Proposition 1A of 2004, the state was required to repay the local government borrowing no later than June 15, 2013. The 2012 Budget Act included \$2.1 billion to fully retire the outstanding obligations, with interest, to be paid from the General Fund, and repayment was made in June of 2013.

Proposition 1A of 2004 also prohibits the state from mandating activities on cities, counties or special districts without providing for the funding needed to comply with the mandates. Beginning in fiscal year 2005-06, if the state does not provide funding for the mandated activity, the requirement on cities, counties or special districts to abide by the mandate is suspended. In addition, Proposition 1A of 2004 expands the definition of what constitutes a mandate on local governments to encompass state action that transfers to cities, counties and special districts financial responsibility for a required program for which the state previously had partial or complete financial responsibility. The state mandate provisions of Proposition 1A of 2004 do not apply to schools or community colleges or to mandates relating to employee rights. The 2013 Budget Act suspends mandates subject to Proposition 1A of 2004 until the 2014-15 fiscal year. The total estimated back cost owed on the suspended mandates is approximately \$888 million. That amount would be payable if the Legislature chose to individually fund all suspended mandates.

Proposition 1A of 2004 further requires the state to reimburse cities, counties, and special districts for mandated costs incurred prior to fiscal year 2004-05 over a term of years. Chapter 72, Statutes of 2005 (AB 138) requires the payment of mandated costs incurred prior to fiscal year 2004-05 to begin in fiscal year 2006-07 and to be paid over a term of 15 years. The 2012-13 Budget, which includes Chapter 32, Statutes of 2012 (SB 1006), defers payment of these claims through the 2014-15 fiscal year and refinances the balance owed over the remaining payment period. The 2013 Budget Act maintains the deferral of the payment. The remaining estimated cost of claims for mandated costs incurred prior to fiscal year 2004-05 is approximately \$900 million.

After School Education Funding (Proposition 49)

An initiative statute, Proposition 49, called the “After School Education and Safety Program Act of 2002,” was approved by the voters on November 5, 2002, and required the state to expand funding for before and after school programs in the state’s public elementary, middle and junior high schools. The increase was first triggered in fiscal year 2006-07, which increased funding for these programs to \$550 million. These funds are part of the Proposition 98 minimum funding guarantee for K-14 education and, in accordance with the initiative, expenditures can only be reduced in certain low revenue years. See “STATE FINANCES – Proposition 98 and K-14 Funding.”

Mental Health Services (Proposition 63)

On November 2, 2004, the voters approved Proposition 63, the Mental Health Services Act, which imposes a 1 percent tax surcharge on taxpayers with annual taxable income of more than \$1 million for purposes of funding and expanding mental health services. Proposition 63 prohibits the Legislature or the Governor from redirecting these funds or from reducing General Fund support for mental health services below the levels provided in fiscal year 2003-04. Chapter 5, Statutes of 2011 (AB 100) allowed the one-time redirection of \$861 million of Proposition 63 funds from the reserve in fiscal year 2011-12 for the Early and Periodic Screening, Diagnosis and Treatment (“EPSDT”) program, mental health managed care, and mental health services for special education students. Commencing in fiscal year 2012-13, the EPSDT program and mental health managed care are funded with “2011 Realignment” funds as the programs are realigned to counties, mental health services for special education students are funded with Proposition 98 General Fund, and all available Proposition 63 funds are distributed for programs eligible under the Mental Health Services Act.

Transportation Financing (Proposition 1A of 2006)

On November 7, 2006, voters approved Proposition 1A of 2006, which had been placed on the ballot by the Legislature as Senate Constitutional Amendment No. 7, to protect Proposition 42 transportation funds from any further suspensions. Provisions of the state Constitution enacted as Proposition 42 in 2002, permitted the suspension of the annual transfer of motor vehicle fuel sales tax revenues from the General Fund to the Transportation Investment Fund if the Governor declared that the transfer would result in a “significant negative fiscal impact” on the General Fund and the Legislature agreed with a two-thirds vote of each house. The new measure modified the constitutional provisions of Proposition 42 in a manner similar to Proposition 1A of 2004, so that if such a suspension were to have occurred, the amount owed by the General Fund would have had to be repaid to the Transportation Investment Fund within three years, and only two such suspensions could have been made within any 10-year period. In fiscal year 2003-04, \$868 million of the scheduled Proposition 42 transfer was suspended, and in fiscal year 2004-05 the full transfer of \$1.258 billion was suspended. Budget Acts for fiscal years 2006-07 through 2010-11 all fully funded the Proposition 42 transfer and partially repaid the earlier suspensions. Chapter 11, Statutes of 2010, in the Eighth Extraordinary Session included an elimination of the state sales tax rate on gasoline and an increase in gasoline excise taxes, effectively removing the revenue subject to these restrictions from the state tax system. However, consistent with the requirements of Proposition 1A of 2006, the 2014-15 Governor’s

Budget includes \$81 million in 2013-14 and \$83 million in 2014-15 to repay a portion of past suspensions. The final payment of \$85 million is scheduled for 2015-16.

Proposition 22 – Local Government Funds

On November 2, 2010, voters approved this measure, called the “Local Taxpayer, Public Safety and Transportation Protection Act of 2010,” which supersedes some parts of Proposition 1A of 2004, prohibits any future action by the Legislature to take, reallocate or borrow money raised by local governments and redevelopment agencies for local purposes, and prohibits changes in the allocation of property taxes among local governments designed to aid state finances or pay for state mandates. The Proposition 1A borrowing done in 2009 was grandfathered. In addition, by superseding Proposition 1A of 2006, the state is prohibited from borrowing sales taxes or excise taxes on motor vehicle fuels for budgetary purposes (but legislation enacted in 2012 clarifies these funds may be used for short-term cash management borrowing), or changing the allocations of those taxes among local governments except pursuant to specified procedures involving public notices and hearings. Any law enacted after October 29, 2009 inconsistent with Proposition 22 is repealed. Proposition 22 jeopardized the use of funds from the gasoline excise tax that had been used in the 2010 Budget Act to offset General Fund debt service cost on highway bonds and for lending to the General Fund. Passage of this measure jeopardized an estimated \$850 million in General Fund relief in fiscal year 2010-11, an amount which would grow to almost \$1 billion by fiscal year 2013-14. The 2011 Budget Act replaced the use of gasoline excise tax for these purposes with truck weight fees and other transportation revenues that may be used for these purposes under Article XIX of the state Constitution. This preserved the 2011 Budget Act allocations for state and local programs while achieving similar levels of General Fund relief to that obtained in the 2010 Budget Act. These debt service offsets were continued in the 2012 and 2013 Budget Acts.

The inability of the state to borrow or redirect property tax funds reduces the state’s flexibility in reaching budget solutions. The state had used these actions for several billion dollars of solutions prior to the enactment of Proposition 22.

Proposition 26 – Increases in Taxes or Fees

On November 2, 2010, voters approved this ballot measure which revises provisions in Articles XIII A and XIII C of the state Constitution dealing with tax increases. The measure specifies that a two-thirds vote of both houses of the Legislature is required for any increase in any tax on any taxpayer, eliminating the prior practice where a tax increase coupled with a tax reduction is treated as being able to be adopted by majority vote. Furthermore, any increase in a fee beyond the amount needed to provide the specific service or benefit is deemed a tax requiring two-thirds vote. Finally, any tax or fee adopted after January 1, 2010 with a majority vote which would have required a two-thirds vote if Proposition 26 were in place would be repealed after one year from the election date unless readopted by the necessary two thirds vote.

Proposition 25 – On-Time Budget Act of 2010

On November 2, 2010, voters approved this measure that is intended to end budget delays by changing the legislative vote necessary to pass the budget bill from two-thirds to a majority

vote and by requiring legislators to forfeit their pay if the Legislature fails to pass the budget bill on time. This measure does not change Proposition 13's property tax limitations in any way. This measure does not change the two-thirds vote requirement for the Legislature to raise taxes. The lower vote requirement also applies to trailer bills that appropriate funds and are identified by the Legislature "as related to the budget in the budget bill." This measure also provides that the budget bill and other bills providing for appropriations related to the budget bill are to take effect immediately upon being signed by the Governor or upon a date specified in the legislation.

Proposition 30 – The Schools and Local Public Safety Protection Act of 2012

On November 6, 2012, voters approved Proposition 30 which provided temporary increases in personal income tax rates for high-income taxpayers and a temporary increase in the state sales tax rate, and specified that the additional revenues will support K-14 public schools and community colleges as part of the Proposition 98 guarantee. Proposition 30 also placed into the state Constitution the current statutory provisions transferring 1.0625 percent of the state sales tax to local governments to fund the "realignment" program for many services including housing criminal offenders. See "STATE FINANCES – Sources of Tax Revenue."

Proposition 39 – The California Clean Energy Jobs Act

On November 6, 2012, voters approved Proposition 39 thereby amending state statutes governing corporation taxes by reversing a provision adopted in 2009 giving corporations an option on how to calculate the portion of worldwide income attributable to California. By requiring corporations to base their state tax liability on sales in California, it is estimated that state revenues would be increased by \$600 million to \$900 million per year starting in 2013-14. The measure also, for five years, dedicates up to an estimated \$550 million per year from this increased income to funding of projects that create energy efficiency and clean energy jobs in California.

FINANCIAL STATEMENTS

The Audited Basic Financial Statements of the State of California for the Year Ended June 30, 2012 (the "Financial Statements") are included as APPENDIX F to this Official Statement and incorporated into this APPENDIX A. The Financial Statements consist of an Independent Auditor's Report, a Management Discussion and Analysis, Basic Financial Statements of the state for the Year Ended June 30, 2012 ("Basic Financial Statements"), and Required Supplementary Information. Only the Basic Financial Statements have been audited, as described in the Independent Auditor's Report. A description of the accounting and financial reporting standards set by the Governmental Accounting Standards Board and used in the Basic Financial Statements is contained in Note 1 of the Basic Financial Statements. The Audited Basic Financial Statements of the State of California for the Year Ended June 30, 2013 are currently expected to be available by mid-April, 2014. The state expects to file unaudited financial statements for the year ended June 30, 2013 with its Annual Reports under its continuing disclosure certificates for outstanding bonds by April 1, 2014.

The State Controller issues a monthly report on General Fund cash receipts and disbursements. These reports are available on the State Controller's website, and are normally released by the 10th day of every calendar month for the period ended on the last day of the prior

month. The State Controller's unaudited reports of General Fund cash receipts and disbursements for the period July 1, 2012 through June 30, 2013 and July 1, 2013 through *February 28, 2014* are included as EXHIBIT 1 and EXHIBIT 2, respectively, to this APPENDIX A.

Periodic reports on revenues and/or expenditures during the fiscal year are issued by the Administration, the State Controller's Office and the LAO. The Department of Finance issues a monthly bulletin, available by accessing the internet website of the Department of Finance (www.dof.ca.gov), which reports the most recent revenue receipts as reported by state departments, comparing those receipts to budget projections. The Administration also formally updates its budget projections three times during each fiscal year, in January, May, and at the time of budget enactment. These bulletins and reports are available on the internet at websites maintained by the agencies and by contacting the agencies at their offices in Sacramento, California. Such bulletins and reports are not part of or incorporated into this APPENDIX A. Investors are cautioned that interim financial information is not necessarily indicative of results for a fiscal year. Information which may appear in this APPENDIX A from the Department of Finance concerning monthly receipts of "agency cash" may differ from the State Controller's reports of cash receipts for the same periods because of timing differences in the recording of in-transit items.

INVESTMENT OF STATE FUNDS

Moneys on deposit in the State Centralized Treasury System are invested by the State Treasurer in the PMIA. As of January 31, 2014, the PMIA held approximately \$36.2 billion of state moneys, and \$20.8 billion invested for about 2,582 local governmental entities through the Local Agency Investment Fund ("LAIF"). The assets of the PMIA as of January 31, 2014 are shown in the following table.

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TABLE 41
Analysis of Pooled Money Investment Account Portfolio^(a)

(Dollars in Thousands)

Type of Security	Amount	Percent of Total
U.S. Treasuries	\$ 32,246,841	56.56%
Federal Agency Debentures	1,984,774	3.48
Certificates of Deposit	9,775,138	17.15
Bank Notes	100,000	0.17
Federal Agency Discount Notes	1,298,933	2.28
Time Deposits	4,547,640	7.98
GNMAs	0	0.00
Commercial Paper	5,523,280	9.69
FHLMC/REMICs	140,682	0.25
AB 55 Loans	358,340	0.63
General Fund Loans	885,900	1.55
Other	<u>149,896</u>	<u>0.26</u>
Total	\$ 57,011,424	100.00%

^(a) Totals may not add due to rounding.

Source: State of California, Office of the State Treasurer.

The State's Treasury operations are managed in compliance with the California Government Code and according to a statement of investment policy which sets forth permitted investment vehicles, liquidity parameters and maximum maturity of investments. The PMIA operates with the oversight of the PMIB. The LAIF portion of the PMIA operates with the oversight of the Local Agency Investment Advisory Board (consisting of the State Treasurer and four other appointed members).

The PMIA is not invested, nor has it ever been invested, in structured investment vehicles or collateralized debt obligations. The PMIA portfolio performance, and the PMIA's holdings are displayed quarterly on the State Treasurer's website and may be accessed under PMIB Quarterly Reports. The PMIA is not currently invested in auction rate securities.

The State Treasurer does not invest in leveraged products or inverse floating rate securities. The investment policy permits the use of reverse repurchase agreements subject to limits of no more than 10 percent of the PMIA. All reverse repurchase agreements are cash matched either to the maturity of the reinvestment or an adequately positive cash management date which is approximate to the maturity of the reinvestment.

The average life of the investment portfolio of the PMIA as of January 31, 2014 was 221 days.

OVERVIEW OF STATE GOVERNMENT

Organization of State Government

The state Constitution provides for three separate branches of government: the legislative, the judicial and the executive. The state Constitution guarantees the electorate the right to make basic decisions, including amending the state Constitution and local government

charters. In addition, the state voters may directly influence state government through the initiative, referendum and recall processes. The state Constitution provides for mechanisms through which it may be amended or revised.

California's Legislature consists of a 40-member Senate and an eighty-member Assembly. Assembly members are elected for two-year terms, and Senators are elected for four-year terms. Before passage of Proposition 28 on June 5, 2012, Assembly members were limited to three terms in office and Senators to two terms. Proposition 28 reduced the total amount of time a person may serve in the Legislature from 14 to 12 years, but allows a person to serve a total of 12 years in either the Assembly, the Senate, or a combination of both. The new term limits law applies only to members of the Legislature elected after the measure was passed.

The Legislature meets almost year round for a two-year session. The Legislature employs the Legislative Analyst, who provides reports on state finances, among other subjects. The Office of the California State Auditor, an independent office since 1993, annually issues an auditor's report based on an examination of the General Purpose Financial Statements of the State Controller, in accordance with generally accepted accounting principles. See "FINANCIAL STATEMENTS."

The Governor is the chief executive officer of the state. The Governor presents the annual budget and traditionally presents an annual package of bills constituting a legislative program. In addition to the Governor, state law provides for seven other statewide elected officials in the executive branch. The Governor and the other statewide officials may be elected for up to two four-year terms. The current elected statewide officials, their party affiliation and the dates on which they were first elected are as follows:

Office	Name	Party Affiliation	First Elected
Governor	Edmund G. Brown Jr.	Democrat	2010*
Lieutenant Governor	Gavin Newsom	Democrat	2010
Controller	John Chiang	Democrat	2006
Treasurer	Bill Lockyer	Democrat	2006
Attorney General	Kamala D. Harris	Democrat	2010
Secretary of State	Debra Bowen	Democrat	2006
Superintendent of Public Instruction	Tom Torlakson	Democrat	2010
Insurance Commissioner	Dave Jones	Democrat	2010

* Previously served as Governor 1975-83, prior to term limit law.

Effective July 1, 2013, by way of the Governor's Reorganization Plan, in addition to other entities such as the Department of Finance, the executive branch is principally administered through the following agencies and Secretaries:

1. Business, Consumer Services and Housing,
2. Government Operations,
3. Corrections and Rehabilitation,
4. Labor and Workforce Development,

5. Health and Human Services,
6. Environmental Protection,
7. Natural Resources,
8. Food and Agriculture,
9. Transportation, and
10. Veterans Affairs.

In addition, some state programs are administered by boards and commissions, such as The Regents of the University of California, Public Utilities Commission, Franchise Tax Board and California Transportation Commission, which have authority over certain functions of state government with the power to establish policy and promulgate regulations. The appointment of members of boards and commissions is usually shared by the Legislature and the Governor, and often includes ex officio members.

Higher Education

California has a comprehensive system of public higher education comprised of three segments: the University of California, the California State University System and California Community Colleges. The University of California provides undergraduate, graduate and professional degrees to students, awarding 63,523 degrees in the 2012-13 school year. The ten University of California campuses and the Hastings College of Law enrolled 239,357 full time students in the 2012-13 school year. The California State University provides undergraduate and graduate degrees, awarding 101,209 degrees in the 2012-13 school year. The California State University enrolled 358,794 full-time students at the 23 campuses in the 2012-13 school year.

The third segment consists of 112 campuses operated by 72 community college districts, which provide associate degrees and certificates to students. Additionally, students may attend California community colleges (“CCCs”) to meet basic skills and other general education requirements prior to transferring to a four-year undergraduate institution. The CCCs awarded 167,946 associate degrees and certificates in the 2012-13 school year. For the 2012-13 school year, approximately 1.1 million full-time equivalent students were enrolled at CCCs.

Employee Relations

The 2014-15 Governor’s Budget estimates the state work force for fiscal year 2014-15 at approximately 355,000 positions, of which approximately 136,000 positions represent state employees of the legislative and judicial branches of government and institutions of higher education. Of the remaining positions, over 80 percent are subject to collective bargaining and less than 20 percent are excluded from collective bargaining. State law provides that state employees, defined as any civil service employee of the state and teachers under the jurisdiction of the Department of Education or the Superintendent of Public Instruction, and excluding certain other categories, have a right to form, join, and participate in the activities of employee organizations for the purpose of representation on all matters of employer-employee relations. Once a bargaining unit (“BU”) selects an employee organization, only that organization can represent those employees.

The scope of representation is limited to wages, hours, and other terms and conditions of employment. Representatives of the Governor are required to meet and confer in good faith and endeavor to reach agreement with the employee organization and, if an agreement is reached, to prepare a memorandum of understanding (“MOU”) and present it to the Legislature for ratification. The Governor and the recognized employee organization are authorized to agree mutually on the appointment of a mediator for the purpose of settling any disputes between the parties, or either party could request the Public Employment Relations Board to appoint a mediator.

There are 21 collective BUs that represent state employees. The Service Employees International Union is the exclusive representative for 9 of the 21 BUs, or approximately 50 percent of those represented employees subject to collective bargaining. The International Union of Operating Engineers is the exclusive representative for 2 of the 21 collective BUs. The remaining BUs have their own exclusive representative. Eighteen of the state’s 21 BUs have an existing MOU. The following table lists the state’s 21 BUs, their exclusive representatives, membership levels, and MOU expiration dates.

TABLE 42
Collective Bargaining Units

Unit	Description	Full-Time Equivalents^(a)	MOU Expiration
1, 3, 4, 11, 14, 15, 17, 20, and 21	Service Employees International Union, Local 1000: Various California Attorneys, Administrative Law Judges & Hearing Officers in State Employment: Attorneys and Administrative Law Judges	91,078	7/1/2016
2	California Association of Highway Patrolmen: Highway Patrol	3,755	7/1/2013 ^(b)
5	California Correctional Peace Officers Association: Corrections	6,635	7/3/2018
6	California Statewide Law Enforcement Association: Protective Services and Public Safety	28,357	7/2/2015
7	California Department of Forestry Firefighters: Firefighters	6,780	7/1/2016
8		4,754	7/1/2017
9	Professional Engineers in California Government: Professional Engineers	10,824	7/1/2015
10	California Association of Professional Scientists: Professional Scientists	2,768	7/1/2013 ^(b)
12	International Union of Operating Engineers: Craft and Maintenance	10,819	7/1/2015
13	International Union of Operating Engineers: Stationary Engineers	936	7/1/2013 ^(b)
16	Union of American Physicians and Dentists: Physicians, Dentists, and Podiatrists	1,517	7/1/2016
18	California Association of Psychiatric Technicians: Psychiatric Technicians	5,413	7/1/2016
19	American Federation of State, County and Municipal Employees: Health and Social Services/Professional	<u>4,859</u>	7/1/2016
Total		178,494	

^(a) Full-Time equivalents are from the Table 183, State Controller’s Office, April 2013.

^(b) While the state and the affected BUs continue to negotiate expired MOUs, such MOUs continue in effect until replaced or extended pursuant to Government Code 3517.8.

Source: Department of Human Resources

The following are major changes in employee compensation and terms of employment in 2013-14, 2014-15, and 2015-16 as a result of the 2013 Budget Act, current MOUs, enacted pension reform legislation, and administratively established compensation adjustments for excluded employees:

Employee contributions of 0.5 percent of base salary towards prefunding other postemployment retirement benefits for BUs 12 and 16 effective July 1, 2013.

State contribution of an additional 2 percent of base salary towards prefunding other postemployment retirement benefits for BU 5 effective July 1, 2013.

BUs 5, 8, 12, 16, 18, 19, and excluded employees associated with BUs 5 and 8 received restructured pay scales that added a top step adjustment of 2 to 5 percent on January 1, 2012. The remaining BUs (1, 2, 3, 4, 6, 7, 9, 10, 11, 13, 14, 15, 17, 20 and 21) and excluded employees received restructured pay scales that added a top step of 2 to 5 percent on July 1, 2013.

BU 5 employees and the related excluded employees received a 4 percent General Salary Increase (GSI), effective July 1, 2013.

State contribution, on behalf of BU 5 employees and the related excluded employees, of an additional 1.9 percent of base salary towards prefunding other post-employment retirement benefits, effective July 1, 2013. This contribution shall be in addition to the contributions already being made.

State contribution of an additional 1.9 percent of base salary towards prefunding other post-employment retirement benefits for BU 5 employees and the related excluded employees, effective July 1, 2015.

BUs 6, 7, and 9 will receive a GSI ranging from 3 to 4 percent between January 1 and July 1, 2015.

The following salary increases are contingent on projected state revenues at the 2014-15 May Revision to the Governor's Budget being sufficient to fully fund existing statutory and constitutional obligations, existing fiscal policy, and the cost of providing the salary increases. This determination is referred to as the "trigger," and shall be at the sole discretion of the Director of Finance. The Governor's Budget assumes the necessary conditions for the trigger-based salary increases will be met and therefore proposes \$173.1 million (\$82.4 million General Fund) to fund them. A final determination will be made when the May Revision is released based on the latest revenue projections and updated expenditure information available.

BU 12 will receive a one-time bonus, effective July 1, 2014, and a 3 percent salary increase, effective July 1, 2015, dependent on the trigger. If the trigger is not met, employees will receive a 3.25 percent salary increase, effective July 1, 2015.

BUs 1, 3, 4, 11, 14, 15, 16, 17, 18, 19, 20, and 21 will receive a 2 percent salary increase, effective July 1, 2014, and a 2.5 percent salary increase, effective July 1, 2015, dependent on the trigger. If the trigger is not met, employees will receive a salary increase of 4.5 percent, effective July 1, 2015, with minor exceptions.

Additionally, the Administration is proposing the same 2 percent salary increase negotiated for the majority of rank and file members described above to unrepresented state managers and supervisors to avoid salary compaction issues. Managers and supervisors associated with BU 5 and BU 6 are proposed to receive the same salary adjustment extended to their rank and file counterparts (6.2 percent on July 1, 2014 and 4 percent on January 1, 2015, respectively). The Governor's Budget includes \$98.6 million (\$40.3 million General Fund) in 2014-15 for these salary increases.

The Governor's Budget also includes funding to address salary parity and inequity issues involving specific state managers and supervisors, particularly related to scientists and engineers.

With the passage of the Public Employees' Pension Reform Act of 2013, state employees in designated bargaining units and associated excluded employees started making additional payroll contributions to their pension plans on July 1, 2013. Generally, the additional employee contribution ranges from 1 to 3 percent, some of which are phased in over a two-year period.

The 2014-15 Governor's Budget includes \$108.4 million (\$73.8 million General Fund) directed toward the state's unfunded pension liability to reflect the savings resulting from the increased employee contributions.

ECONOMY AND POPULATION

Introduction

California's economy, the largest among the 50 states and one of the largest in the world, has major components in high technology, trade, entertainment, agriculture, manufacturing, tourism, construction and services. California followed the nation's path through the recession and into the recovery. California labor markets deteriorated dramatically during the latter half of 2008 and the first nine months of 2009, suffering their worst losses on record. From July 2007 through September 2009, the state lost nearly 1.4 million nonfarm jobs. These losses switched to very modest gains during 2010 and 2011, which accelerated in 2012. California has gained 681,500 jobs from September 2009 through December 2012. See "PROPOSED FISCAL YEAR 2014-15 BUDGET – Development of Revenue Estimates."

Population, Labor Force and Demographic Trends

In 2013 California's population reached 38.2 million residents. California's population gain over the ten years (2003-2013) is 2.8 million persons. To put this in perspective, California added more residents between 2003 and 2013 than the total 2010 population of each of the seventeen least populated states. While the last few years have seen relatively slow growth, this short-term trend is beginning to change. As California's economy continues to improve and employment picks up, California will continue to see stronger population gains.

California's population is projected to be 38,548,000 in July 2014 and 38,902,000 by July 2015, which allow for growth rates of 0.90 and 0.92 percent respectively. The forecast further assumes that through the next five years, the state will grow at a slightly higher rate than over the last few years, averaging over 360,000 residents annually through 2018. Natural increase will account for most of the growth during this time. Net migration is projected to gradually increase

as economic conditions continue to improve. By July 2018, California will have added 1.8 million people and have a population of over 40.0 million, a five-year growth rate of 4.7 percent.

The dependency ratio is an economic measure which approximates dependency by dividing the dependent-age population (under 18 plus 65 and over) by the working-age (18 to 64) population. The ratio represents the dependent age population per 100 working-age population. The dependency ratio for California's 2010 population stood at 57.1, compared to 59.2 for the remainder of the United States. The dependency ratio ignores labor force participation rates, as well as employment and unemployment levels.

The demographic phenomenon of the baby-boom began in 1946 and ended in 1964, so the first baby-boomers began to turn 65 in 2011. California will experience large growth in the 65 and over age group for the next two decades, as will the United States and much of the world. However, California enjoys a more diverse population that remains younger than most other states in the union. According to the 2010 Census, California's 65 and over age cohort comprised 11.4 percent of the state's population; in the remainder of the United States, the 65 and over groups accounted for 13.3 percent of the population. Only five states have a lower percentage of the population who are 65 years of age or older.

As the state's growth patterns change, the age and race distribution of California's population continue to transform. By early 2014, for the first time since California became a state, the Hispanic population will become the largest group in California. This shift is due primarily to variations in demographic patterns, including fertility, age structure, and migration. In July 2013, of the non-Hispanic White population, 43 percent were at least 50 years of age, while 19 percent of Hispanics were age 50 or older.

Population growth rates vary significantly by age group. The state's projected total five-year growth rate of 4.7 percent is higher than the anticipated 3 percent growth in the preschool-age group. The school-age group will increase by 0.2 percent, and the college-age group will decrease by 4.5 percent. The working-age population will grow by 871,000 or 4.3 percent. The population of the retirement-age group, those 65 and older, will expand rapidly (20.7 percent). The retirement-age growth will be concentrated in the 65 through 74 age cohort, with a growth rate of 26.5 percent.

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The following table shows California's population data for 2002 through 2013.

TABLE 43
Population 2002-2013

Year	California Population^(a)	Increase Over Preceding Year	United States Population^(a)	Increase Over Preceding Year	California as % of United States
2002	34,938,290	1.2%	287,803,914	1.0%	12.1
2003	35,388,928	1.3	290,326,418	0.9	12.2
2004	35,752,765	1.0	293,045,739	0.9	12.2
2005	35,985,582	0.7	295,753,151	0.9	12.2
2006	36,246,822	0.7	298,593,212	1.0	12.1
2007	36,552,529	0.8	301,579,895	1.0	12.1
2008	36,856,222	0.8	304,374,846	0.9	12.1
2009	37,077,204	0.6	307,006,550	0.9	12.1
2010	37,309,404	0.6	309,326,295	0.8	12.1
2011	37,570,112	0.7	311,582,564	0.7	12.1
2012	37,872,431	0.8	313,873,685	0.7	12.1
2013	38,204,597	0.9	316,128,839	0.7	12.1

^(a) Population as of July 1.

Source: U. S. figures from U.S. Department of Commerce, Bureau of the Census; California figures from State of California, Department of Finance.

The following table presents civilian labor force data for the resident population, age 16 and over, for the years 2002 to 2013.

TABLE 44
Labor Force 2002-2013
(Thousands)

Year	Labor Force	Employment	Unemployment Rate	
			California	United States
2002	17,344	16,181	6.7%	5.8%
2003	17,391	16,200	6.8	6.0
2004	17,444	16,355	6.2	5.5
2005	17,545	16,592	5.4	5.1
2006	17,687	16,821	4.9	4.6
2007	17,921	16,961	5.4	4.6
2008	18,207	16,894	7.2	5.8
2009	18,216	16,151	11.3	9.3
2010	18,331	16,064	12.4	9.6
2011	18,405	16,237	11.8	8.9
2012	18,495	16,560	10.5	8.1
2013p/	18,608	16,965	8.8	7.4

p/ Preliminary until March 7, 2014.

Source: State of California, Employment Development Department.

Employment, Income, Construction and Export Growth

The following table shows California's nonfarm payroll employment distribution and growth for 2003 and 2013.

TABLE 45
Nonfarm Payroll Employment by Major Sector
2003 and 2013
(Thousands)

Industry Sector	Employment		Distribution of Employment	
	2003	2013 ^{p/}	2003	2013 ^{p/}
Mining and Logging	22.2	29.6	0.2%	0.2%
Construction	796.8	619.5	5.5	4.2
<i>Manufacturing</i>				
Nondurable Goods	566.0	465.8	3.9	3.2
High Technology	394.6	341.2	2.7	2.3
Other durable	583.9	442.9	4.1	3.0
Trade, Transportation & Utilities	2,716.3	2,762.7	18.9	18.9
Information	476.1	434.4	3.3	3.0
Financial Activities	878.8	786.8	6.1	5.4
Professional & Business Services	2,085.3	2,302.1	14.5	15.7
Educational & Health Services	1,542.9	1,918.7	10.7	13.1
Leisure & Hospitality	1,400.1	1,668.2	9.7	11.4
Other Services	504.3	510.2	3.5	3.5
<i>Government</i>				
Federal Government	255.4	243.9	1.8	1.7
State & Local Government	2,170.7	2,116.3	15.1	14.5
TOTAL	14,393.5	14,642.4	100.0%	100.0%

Source: State of California, Employment Development Department. (Note: Figures may not add due to rounding.)

^{p/} Preliminary until March 7, 2014.

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The following tables show California's total and per capita income patterns for selected years.

TABLE 46
Total Personal Income in California 2001-2012^(a)
(Dollars in Millions)

Year	Total Personal Income	% Change(b)	California % of U.S.
2001	\$1,174,489	3.4%	13.1%
2002	1,193,375	1.6	13.0
2003	1,244,351	4.3	13.1
2004	1,321,609	6.2	13.2
2005	1,396,173	5.6	13.2
2006	1,499,452	7.4	13.2
2007	1,564,441	4.3	13.0
2008	1,596,282	2.0	12.8
2009	1,536,430	-3.7	12.7
2010	1,579,148	2.8	12.7
2011	1,683,204	6.6	12.8
2012	1,768,039	5.0	12.9

^(a) Estimates for 2001 forward reflect the results of the comprehensive revision to the national income and product accounts (NIPAs) released in July 2013.

^(b) Change from prior year.

Note: omits income for government employees overseas.

Source: U.S. Department of Commerce, Bureau of Economic Analysis

TABLE 47
Per Capita Personal Income 2001-2012^(a)

Year	California	% Change(b)	United States	% Change(b)	California % of U.S.
2001	\$34,063	2.0%	\$31,524	4.0%	108.1%
2002	34,222	0.5	31,798	0.9	107.6
2003	35,298	3.1	32,676	2.8	108.0
2004	37,150	5.2	34,300	5.0	108.3
2005	38,969	4.9	35,888	4.6	108.6
2006	41,627	6.8	38,127	6.2	109.2
2007	43,157	3.7	39,804	4.4	108.4
2008	43,609	1.0	40,873	2.7	106.7
2009	41,569	-4.7	39,357	-3.7	105.6
2010	42,297	1.8	40,163	2.0	105.3
2011	44,666	5.6	42,298	5.3	105.6
2012	46,477	4.1	43,735	3.4	106.3

^(a) Estimates for 2001 forward reflect the results of the comprehensive revision to the national income and product accounts (NIPAs) released in July 2013.

^(b) Change from prior year.

Note: omits income for government employees overseas.

Source: U.S. Department of Commerce, Bureau of Economic Analysis.

The following tables show California's residential and non-residential construction.

TABLE 48
Residential Construction Authorized By Permits
2001-2013

Year	Units			Valuation ^(a) (Dollars in Millions)
	Total	Single	Multiple	
2001	148,757	106,902	41,855	\$28,804
2002	167,761	123,865	43,896	33,305
2003	195,682	138,762	56,920	38,968
2004	212,960	151,417	61,543	44,777
2005	208,972	155,322	53,650	47,138
2006	164,280	108,021	56,259	38,108
2007	113,034	68,409	44,625	28,621
2008	64,962	33,050	31,912	18,072
2009	36,421	25,454	10,967	12,037
2010	44,762	25,526	19,236	13,731
2011	47,092	21,538	25,554	14,356
2012	57,961	27,406	30,555	16,451
2013 ^{p/}	82,674	36,281	46,393	22,328

^(a) Valuation includes additions and alterations.

^{p/} Preliminary.

Source: Construction Industry Research Board.

TABLE 49
Non-residential Construction 2001-2013

(Dollars in Thousands)

Year	Commercial	Industrial	Other	Additions and Alterations	Total
2001	\$6,195,368	\$1,552,047	\$2,584,321	\$6,421,551	\$16,753,287
2002	5,195,348	1,227,754	2,712,681	5,393,329	14,529,112
2003	4,039,561	1,320,222	2,954,039	5,601,117	13,914,939
2004	5,105,541	1,456,283	3,100,982	6,026,567	15,689,373
2005	5,853,351	1,693,373	3,818,100	6,900,709	18,265,533
2006	7,733,068	1,760,888	3,873,055	7,741,610	21,108,621
2007	8,812,083	1,450,875	3,496,471	8,782,424	22,541,853
2008	6,513,610	938,081	2,983,640	8,776,285	19,211,616
2009	1,919,763	359,868	1,984,534	6,602,103	10,866,268
2010	1,990,358	358,338	1,937,166	6,913,901	11,199,763
2011	2,213,037	478,896	2,224,685	8,144,510	13,061,128
2012	3,215,903	1,409,808	2,382,790	7,626,971	14,635,471
2013 ^{p/}	5,200,328	1,075,472	6,250,539	8,836,957	21,363,296

^{p/} Preliminary

Source: Construction Industry Research Board.

The following table shows changes in California's exports for the period from 2001 through 2013.

TABLE 50
Exports through California Ports 2001-2013

(Dollars in Millions)

Year	Exports ^(a)	% Change ^(b)
2001	\$126,960.0	-14.4%
2002	111,305.1	-12.3
2003	113,351.0	1.8
2004	123,097.7	8.6
2005	129,929.2	5.5
2006	147,766.9	13.7
2007	159,357.1	7.8
2008	170,313.8	6.9
2009	137,087.2	-19.5
2010	168,412.8	22.9
2011	189,371.8	12.4
2012	191,702.8	1.2
2013	201,815.8	5.3

(a) "Free along ship" value basis.

(b) Change from prior year.

Source: U.S. Department of Commerce, Bureau of the Census

LITIGATION

The state is a party to numerous legal proceedings. The following describes litigation matters that are pending with service of process on the state accomplished and have been identified by the state as having a potentially significant fiscal impact upon the state's revenues or expenditures. The state makes no representation regarding the likely outcome of these litigation matters.

The following description was developed by the state with the participation of the Office of the Attorney General and other state entities. The Office of the Attorney General does not represent the state, its subdivisions, departments, agencies and other units in all litigation matters, and accordingly there may be litigation matters of which the Office of the Attorney General is not aware. The state does not conduct a docket search of federal or state court litigation filings to identify pending litigation and no inquiry has been made into pending administrative proceedings. There may be litigation and administrative proceedings with potentially significant fiscal impacts that have not been described below.

Budget-Related Litigation

Actions Challenging Cap and Trade Program Auctions

In *California Chamber of Commerce, et al. v. California Air Resources Board*, (Sacramento County Superior Court, Case No. 34-2012-80001313), business interests and a taxpayer challenge the authority of the California Air Resources Board to conduct auctions under the state's cap and trade program and allege that the auction revenues are an unconstitutional tax

under the state Constitution. A second lawsuit raising substantially similar claims, *Morning Star Packing Co., et al. v. California Air Resources Board* (Sacramento County Superior Court, Case No. 34-2013-80001464), was consolidated with the *Chamber of Commerce* matter. The trial court ruled for the Board, finding that it had authority to conduct the auctions, and that the auction does not constitute an unconstitutional tax. Petitioners have filed notices of appeal.

Actions Challenging School Financing

In *Robles-Wong, et al. v. State of California* (Alameda County Superior Court, Case No. RG-10-515768) and *California Teachers Association (“CTA”) Complaint in Intervention*, plaintiffs challenge the state’s “education finance system” as unconstitutional. Plaintiffs, consisting of 62 minor school children, various school districts, the California Association of School Administrators, the California School Boards Association and CTA, allege the state has not adequately fulfilled its constitutional obligation to support its public schools, and seek an order enjoining the state from continuing to operate and rely on the current financing system and to develop a new education system that meets constitutional standards as declared by the court. It is currently unknown what the fiscal impact of this matter might be upon the General Fund. In a related matter, *Campaign for Quality Education, et al. v. State of California* (Alameda County Superior Court, Case No. RG-10-524770), plaintiffs also challenge the constitutionality of the state’s education finance system. The court issued a ruling that there was no constitutional right to a particular level of school funding. The court allowed plaintiffs to amend their complaint with respect to alleged violation of plaintiffs’ right to equal protection. Plaintiffs in each of these matters elected not to amend, and both matters were dismissed by the trial court. Plaintiffs in each matter appealed (Court of Appeal, First Appellate District, Case Nos. A134423, A134424).

Plaintiff in *California School Boards Association v. State of California* (Alameda County Superior Court, Case No. RG-11-554698), challenges the use of block grant funding to pay for education mandates in the 2012 Budget Act and associated trailer bills. The amended complaint also contends that recent changes to the statutes that control how education mandates are directed and funded violate the requirements of the state Constitution that the state pay local school districts for the costs of state mandated programs. If the court declares that the state has failed to properly pay for mandated educational programs, the state will be limited in the manner in which it funds education going forward.

Actions Challenging Statutes Which Reformed California Redevelopment Law

In *California Redevelopment Association, et al. v. Matosantos, et al.* (California Supreme Court, Case No. S194861), the California Supreme Court upheld the validity of legislation (“ABx1 26”) dissolving all local Redevelopment Agencies (“RDAs”) and invalidated a second law (“ABx1 27”) that would have permitted existing RDAs to convert themselves into a new form of RDA and continue to exist, although they would have to pay higher fees to school, fire and transit districts to do so.

A second case challenging the constitutionality of these statutes, *City of Cerritos, et al. v. State of California* (Sacramento County Superior Court, Case No. 34-2011-80000952) raises the same theories advanced in *Matosantos*, and also contains challenges based on claimed violations of the single subject rule and the contracts clause, the statutes being outside scope of the

proclamation calling the Legislature into special session, and the failure to obtain a 2/3 vote to pass the statutes. The trial court denied the petitioners' motion for a preliminary injunction seeking to block implementation of ABx1 26. Plaintiffs appealed (Court of Appeal, Third Appellate District, Case No. C070484). Plaintiffs' request to stay portions of ABx1 26 was denied by the appellate court.

There are over 100 pending actions that challenge implementation of the statutory process for winding down the affairs of the RDAs, asserting a variety of claims including constitutional claims. Some of the pending cases challenge AB 1484, which requires successor agencies to the former RDAs to remit by July 2012 certain property tax revenues for fiscal year 2011-12 that the successor agency had received, or face a penalty. Some cases challenge other provisions in ABx1 26 or AB 1484 that require successor agencies to remit various funds of former RDAs. One such case, *City of Brentwood, et al. v. California Department of Finance, et al.* (Sacramento County Superior Court, Case No. 34-2013-80001568), challenges provisions that retroactively invalidate transfers of funds from a former RDA to the city or county that created the RDA, and require redistribution of those funds. Another case, *League of California Cities, et al. v. Matosantos, et al.* (Sacramento County Superior Court, Case No. 34-2012-80001275), challenges the statutory mechanisms for the Department of Finance or the county auditor-controller to recover these disputed amounts. The trial court denied the petition for a writ in this matter but on reconsideration, granted the writ in part, striking down provisions that allowed the state to withhold a city's sales and use tax. Another matter asserting similar arguments was heard by the trial court on September 20, 2013, and the court issued a ruling in favor of the state, finding all of the challenged statutes facially constitutional. *City of Bellflower, et al. v. Matosantos, et al.* (Sacramento County Superior Court, Case No. 34-2012-80001269). Petitioners filed a notice of appeal. Other cases challenge the implementation of ABx1 26, contending that various obligations incurred by the RDAs are enforceable obligations entitled to payment from tax revenues under ABx 1 26. In *Affordable Housing Coalition v. Sandoval* (Sacramento County Superior Court, Case No. 34 2012-80001158), plaintiffs argue that all former RDAs had obligations to pay for affordable housing that should be funded going forward on an implied contracts theory. The court denied a motion for class action status in this matter.

Actions Regarding Furlough of State Employees

In several cases, petitioners challenged Governor Schwarzenegger's executive orders directing the furlough without pay of state employees. The first order, issued on December 19, 2008, directed furloughs for two days per month, effective February 1, 2009 through June 30, 2010. The second, issued on July 1, 2009, required a third furlough day per month, effective through June 30, 2010. On July 28, 2010, Governor Schwarzenegger issued a new executive order requiring furloughs for three days per month beginning August 1, 2010, until a new 2010 Budget Act was adopted and the Director of the Department of Finance determined that the state had sufficient cash flow to pay for essential services.

On October 4, 2010, the California Supreme Court, ruling in three consolidated cases, upheld the validity of the two day per month furloughs implemented by the Governor's December 2008 order on the ground that the Legislature had ratified these furloughs in enacting the 2008 budget revision. *Professional Engineers in California Government ("PECG"), et al. v. Schwarzenegger, et al.* (California Supreme Court, Case No. S183411).

Most of the remaining cases that challenge the two furlough orders issued in July 2009 and/or July 2010 have been dismissed or settled. The pending cases include the following:

Two cases challenge the furloughs of certain categories of employees, such as those paid from funds other than the General Fund or who otherwise assert a claim not to be furloughed on a basis outside of the rationale of the California Supreme Court decision. These two cases are *PECG v. Schwarzenegger, et al.* (Alameda County Superior Court, Case No. RG 10 494800) and *California Association of Professional Scientists v. Schwarzenegger, et al.* (Alameda County Superior Court, Case No. RG-10-530845). The trial court granted the petition in part, finding that two furlough days in March 2011, were unlawful for specified employees. The state appealed (Court of Appeal, First Appellate District, Case No. A136338).

In *Horton v. Brown, et al.* (Sacramento County Superior Court, Case No. 34-2012-00125438), plaintiff asserts a class action on behalf of all gubernatorial and certain other appointees. The complaint alleges that such appointees were exempt from civil service rules, and therefore should not have been furloughed. The trial court granted the state's motion to strike certain claims and the appellate court rejected the plaintiff's appeal (Court of Appeal, Third District, Case No. C073117). Because the putative class is limited, any fiscal impact on the state's General Fund is expected to be modest.

In *PECG, et al. v. Brown et al.* (Alameda County Superior Court, Case No. RG-13-673444) PECG challenges the implementation of the 2012 furlough program, for the period of July 1, 2012 through June 2013, alleging an unlawful impairment of contractual rights in the bargaining agreement. The trial court ruled for the state and petitioners filed a notice of appeal (Court of Appeal, First Appellate District, Case No. A141028).

In *Vent v. Brown, et al.* (Sacramento County Superior Court, Case No. 34-2013-80001576), an individual state employee challenges both Governor Schwarzenegger's furlough order and the 2012 furlough program and seeks back pay for herself and other attorneys employed by the state.

Action Challenging Use of Mortgage Settlement Proceeds

In National Asian American Coalition, et al. v. Brown, et al. (Sacramento County Superior Court, Case No. 34-2014-80001784), three non-profit organizations allege that approximately \$369 million received by the state in 2012 in connection with the nationwide settlement between states and certain mortgage servicers was deposited in a special fund intended to provide assistance to California homeowners, but that such settlement monies were instead used for other purposes in the fiscal year 2012-13 budget. The plaintiffs allege the use of the settlement monies was inconsistent with the terms of the settlement agreement and California law, and seek to compel state officials to return the monies to the special fund.

Tax Cases

Six actions have been filed contending that the Legislature's modification of Revenue and Taxation Code Section 25128, which implemented the double-weighting of the sales factor in California's apportionment of income formula for the taxation of multistate business entities, is invalid and/or unconstitutional. *Kimberly-Clark Worldwide, Inc., et al. v. Franchise Tax*

Board (San Francisco County Superior Court, Case No. CGC-10-495916); *Gillette Company and Subsidiaries v. Franchise Tax Board* (San Francisco County Superior Court, Case No. CGC-10-495911); *Procter & Gamble Manufacturing Company & Affiliates v. Franchise Tax Board* (San Francisco County Superior Court, Case No. CGC 10 495912); *Sigma-Aldrich, Inc. and Affiliates v. Franchise Tax Board* (San Francisco County Superior Court, Case No. CGC-10-496437); *RB Holdings (USA), Inc. v. Franchise Tax Board* (San Francisco County Superior Court, Case No. CGC-10-496438); and *Jones Apparel Group v. Franchise Tax Board* (San Francisco County Superior Court, Case No. CGC-10-499083), now consolidated in one matter, collectively referred to as *Gillette Company v. Franchise Tax Board*. Plaintiffs contend that the single-weighted sales factor specified in Section 25128 prior to amendment was contained within the Multistate Tax Compact (“Compact”) and therefore cannot be modified without repealing the legislation that enacted the Compact. An adverse ruling in these cases would affect multiple taxpayers and create potential exposure to refund claims in excess of \$750 million. The trial court ruled for the state in each of these matters, but, on appeal, the trial court judgment was reversed (Court of Appeal, First Appellate District, Case No. A130803). The appellate court held that the Compact was valid and the state was bound by its provisions for the tax years at issue because the state had not withdrawn from the Compact. The court also held that in attempting to override the contractual terms of the Compact, section 25128 violated the constitutional protections against impairment of contract. The California Supreme Court granted the state’s petition for review (California Supreme Court Case No. S206587). See “STATE FINANCES – Sources of Tax Revenue – Corporation Tax.”

A pending case challenges the fee imposed by the state tax code upon limited liability companies (“LLCs”) registered in California, alleging that it discriminates against interstate commerce and violates the U.S. and the state Constitutions, is an improper exercise of the state’s police powers, and has been misapplied by the Franchise Tax Board. *Bakersfield Mall LLC v. Franchise Tax Board* (San Francisco County Superior Court, Case No. CGC-07-462728). *Bakersfield Mall* was filed as a purported class action on behalf of all LLCs operating solely in California. Plaintiff filed an amended complaint to allege that not all of its income is derived solely from sources in California, which would call into question the class plaintiff purports to represent. A second lawsuit that is virtually identical to *Bakersfield Mall* also seeks to proceed as a class action. *CA-Centerside II, LLC v. Franchise Tax Board* (Fresno County Superior Court, Case No. 10 CECG00434). The cases are coordinated for hearing in San Francisco as the *Franchise Tax Board LLC Tax Refund Cases*, Judicial Council Proceeding No. 4742. The coordination trial judge denied the plaintiffs’ joint motion for class certification and the plaintiffs appealed (Court of Appeal, First Appellate District, Case No. A140518). If this immediately appealable order is reversed and the cases proceed as class actions, the claimed refunds could be significant (in excess of \$500 million).

Lucent Technologies, Inc. v. State Board of Equalization (“*Lucent I*”) (Los Angeles County Superior Court, Case No. BC 402036), a tax refund case, involves the interpretation of certain statutory sales and use tax-exemptions relating to computer software and licenses to use computer software that are transferred pursuant to technology transfer agreements. A second case, *Lucent Technologies, Inc. v. State Board of Equalization* (“*Lucent II*”) (Los Angeles County Superior Court, Case No. BC 448715), involving the same issue but for different tax years than in the *Lucent I* matter, was consolidated with the *Lucent I* case. In a similar case, *Nortel Networks Inc. v. State Board of Equalization* (Los Angeles County Superior Court, Case

No. BC 341568), the trial court ruled in favor of plaintiff and the ruling was affirmed on appeal (Court of Appeal, Second Appellate District, Case No. B213415, California Supreme Court, Case No. S190946). The adverse ruling in the *Nortel* matter, unless limited in scope by a decision in the *Lucent* matters, if applied to other similarly situated taxpayers, could have a significant negative impact, in the range of approximately \$300 million annually, on tax revenues. In the *Lucent* matters, the trial court granted plaintiffs' motion for summary judgment and denied the Board of Equalization's motion for summary judgment.

Two pending cases challenge the state's right to require interstate unitary businesses to report their income on a combined basis while allowing intrastate unitary businesses to report the income of each business entity on a separate basis. *Harley Davidson, Inc. and Subsidiaries v. California Franchise Tax Board* (San Diego County Superior Court, Case No. 37-2001-00100846-CU-MC-CTL and Court of Appeal, Fourth Appellate District, Case No. D064241) and *Abercrombie & Fitch Co. & Subsidiaries v. California Franchise Tax Board* (Fresno County Superior Court, Case No. 12 CE CG 03408) challenge the constitutionality of Revenue and Taxation Code Section 25101.15, allowing intrastate unitary businesses the option to report their income on a separate rather than combined basis. The trial court in *Harley Davidson* sustained a demurrer on this issue without leave to amend; the issue is now pending on appeal. Trial in *Abercrombie* is set for February 2015. Should Section 25101.15 be invalidated, a significant amount of otherwise apportionable income from multi-state unitary businesses would be removed from the state taxing power. At this time, it is unknown what future fiscal impact a potential adverse ruling would actually have on corporation taxes (including potentially rebates of previously collected taxes and reduced future tax revenue) because of the uncertainty regarding the number of businesses which currently pay the tax and how taxation on those companies would change as a result of an adverse ruling. However, the fiscal impact could be significant. See "STATE FINANCES – Sources of Tax Revenues – Corporation Tax" for a discussion of corporation taxes. The *Harley Davidson* case also raises the issue raised in the *Gillette* case regarding modification of the apportionment formula for multi-state businesses; resolution of this issue in *Harley Davidson* has been deferred to await the outcome of the issue in *Gillette* (discussed above).

A pending bankruptcy matter, *In re Washington Mutual Inc.* (U.S. Bankruptcy Court, D. Delaware, Case No. 08-12229), involves a taxpayer claim to a refund. The disputed issues involve among others the taxpayer's use of Regulated Investment Companies (RICs) and Real Estate Investment Trusts (REITs) as vehicles to shelter millions of dollars of income from taxation. In the event the issues are decided adversely to the Franchise Tax Board, the matter could result in a significant refund, which could be approximately \$400 million. *The parties are discussing settlement and plan to submit a settlement proposal to the court for approval in early April 2014.*

Environmental Matters

In a federal Environmental Protection Agency ("U.S. EPA") administrative abatement action titled *In the Matter of: Leviathan Mine, Alpine County, California, Regional Water Quality Control Board, Lahontan Region, State of California* (U.S. EPA Region IX CERCLA Docket No. 00-16(a)), the state, as owner of the inactive Leviathan Mine, is a responsible party through the Lahontan Regional Water Quality Control Board ("Regional Board"). The Atlantic

Richfield Company (“ARCO”) is also a responsible party as the successor in interest to the mining company that caused certain pollution of the mine site. The Leviathan Mine site (“Site”) is listed on the U.S. EPA “Superfund” List, and both remediation costs and costs for natural resources damages may be imposed on the state. The alleged bases for the state’s liability are the state’s ownership of the Site and the terms of a 1983 settlement agreement between the Regional Board and ARCO. The Regional Board purchased the Site to abate the pollution and has undertaken certain remedial actions (“Project”), but the U.S. EPA’s decision on the interim and final remedies is pending. ARCO has sued the state, the State Water Resources Control Board, and the Regional Board, seeking to recover past and future clean-up costs, based on the settlement agreement, the state’s ownership of the property, and the Regional Board’s allegedly defective Project. The October 2012 trial date for this matter was postponed until April 2014 to permit the parties to continue settlement negotiations. *Atlantic Richfield Co. v. State of California* (Los Angeles County Superior Court, Case No. BC 380474). It is possible these matters if determined adversely to the state could result in potential liability in the hundreds of millions of dollars.

In *Pacific Lumber Company, et al. v. State of California, et al.* (Sacramento County Superior Court, Case No. 34-2009-00042016), plaintiffs seek damages against the state for an alleged breach of the Headwaters Agreement. The Headwaters Agreement, reached in 1996, involved the sale of certain timberlands by plaintiffs to federal and state agencies. Plaintiffs allege that the state’s environmental regulation of plaintiffs’ remaining timberlands since the Headwaters Agreement constitutes a breach of the Agreement. The state denies plaintiffs’ allegations. The current plaintiffs are successors in interest to the original plaintiffs, who filed a bankruptcy proceeding and have since dissolved. In that proceeding, the debtors claimed that the value of the litigation ranges from \$626 million to \$639 million in the event they could establish liability. It is currently unknown what the fiscal impact of this matter might be upon the General Fund. The trial court granted the state’s motion for summary judgment and the appellate court affirmed (*Avidity Partners, LLC v. State of California*, Court of Appeal, Third Appellate District, Case No. C070255). Plaintiffs’ petition for review was denied by the California Supreme Court (California Supreme Court, Case No. S215786).

In *Consolidated Suction Dredge Mining Cases (Karuk Tribe v. DFG)* (Alameda, Siskiyou, and San Bernardino County Superior Courts), environmental and mining interests challenge the state’s regulation of suction dredge gold mining. After initially prohibiting such mining in the state except pursuant to a permit issued by the Department of Fish and Wildlife (formerly Fish and Game) under specified circumstances, the Legislature subsequently placed a moratorium on all suction dredging until certain conditions are met by the Department. The cases are coordinated for hearing in San Bernardino County Superior Court (Case No. JCPDS4720). One of these matters, *The New 49’ERS, Inc. et al. v. California Department of Fish and Game*, claims that federal law preempts and prohibits state regulation of suction dredge mining on federal land. Plaintiffs, who have pled a class action but have yet to seek certification, claim that as many as 11,000 claims, at a value of \$500,000 per claim, have been taken.

In *City of Colton v. American Promotional Events, Inc., et al.* (Los Angeles County Superior Court, Case No. BC 376008), two defendants in an action involving liability for contaminated groundwater have filed cross complaints seeking indemnification from the state and the Regional Water Quality Control Board in an amount of up to \$300 million. In a related

action, *Emhart Industries v. Regional Water Quality Control Board* (Los Angeles County Superior Court, Case No. BC 472949), another defendant in an action involving liability for contaminated groundwater seeks indemnification from the state and the Regional Water Quality Control Board in an amount up to \$300 million.

Escheated Property Claims

In *Taylor v. Chiang* (U.S. District Court, Eastern District, Case No. S-01-2407 WBS GGH), plaintiffs claim that the state's unclaimed property program violates the United States Constitution and various federal and state laws. They assert that the state has an obligation to pay interest on private property that has escheated to the state, and that failure to do so constitutes an unconstitutional taking of private property. Although the case is styled as a class action, no class has been certified. Plaintiffs also assert that for the escheated property that has been disposed of by the state, plaintiffs are entitled to recover, in addition to the proceeds of such sale, any difference between the sale price and the property's highest market value during the time the state held it; the state asserts that such claims for damages are barred by the Eleventh Amendment. The district court ruled against plaintiffs in a related action, *Suever v. Connell* (U.S. District Court, Northern District, Case No. C03-00156 RS). The Ninth Circuit affirmed and the United States Supreme Court denied review. Meanwhile, the *Taylor* plaintiffs amended their complaint to allege that the Controller applies the Unclaimed Property Law's notice requirements in ways that violate state and federal law, and the district court granted the state's motion to dismiss plaintiffs' claims. Plaintiffs appealed this ruling to the Ninth Circuit.

Actions Seeking Damages for Alleged Violations of Privacy Rights

In *Gail Marie Harrington-Wisely, et al. v. State of California, et al.* (Los Angeles County Superior Court, Case No. BC 227373), plaintiffs seek damages, asserting that the use by the California Department of Corrections and Rehabilitation ("CDCR") of a body-imaging machine to search visitors entering state prisons for contraband violated the rights of the visitors. This matter was certified as a class action. The trial court granted judgment in favor of the state. Plaintiffs' appeal was dismissed (Court of Appeal, Second Appellate District, Case No. B190431) and the trial court denied plaintiffs' motion for attorneys' fees. The parties agreed to a stipulated judgment and dismissed the case subject to further review if CDCR decides to use similar technology in the future. Plaintiffs filed another appeal (Court of Appeal, Second Appellate District, Case No. B248565). If plaintiffs were successful in obtaining an award of damages for every use of the body-imaging machine, damages could be as high as \$3 billion.

Plaintiff in *Gilbert P. Hyatt v. Franchise Tax Board* (State of Nevada, Clark County District Court, Case No. A382999) was subject to an audit by the Franchise Tax Board involving a claimed change of residence from California to Nevada. Plaintiff alleges a number of separate torts involving privacy rights and interference with his business relationships arising from the audit. The trial court ruled that plaintiff had not established a causal relation between the audit and the loss of his licensing business with Japanese companies; the Nevada Supreme Court denied review of this ruling. The economic damages claim exceeded \$500 million. On the remaining claims, the jury awarded damages of approximately \$387 million, including punitive damages, and over \$1 million in attorneys' fees. The total judgment with interest is approximately \$490 million. The state appealed and the Nevada Supreme Court granted a stay

of execution on the judgment pending appeal. The state will vigorously pursue its appeal of this unprecedented award.

Action Regarding Special Education

Plaintiffs in *Morgan Hill Concerned Parents Assoc. v. California Department of Education* (United States District Court, Eastern District of California, No. 2:11-cv-3471-KJM), challenge the oversight and operation by the California Department of Education (“CDE”) of the federal Individuals with Disabilities Education Act (“IDEA”). The complaint alleges that CDE, as the designated State Education Agency, has failed to monitor, investigate, and enforce the IDEA statewide. Under the IDEA, local school districts are the Local Educational Agencies responsible for delivering special education directly to eligible students. The complaint seeks injunctive and declaratory relief, and asks the court to retain jurisdiction to monitor the operation of the IDEA by the state.

Actions Regarding Medi-Cal Reimbursements and Fees

In *Orinda Convalescent Hospital Inc., et al. v. Department of Health Services, et al.* (Sacramento County Superior Court, Case No. 06CS01592), plaintiffs challenge a quality assurance fee (“QAF”) charged to skilled nursing facilities that was enacted in 2004, alleging violations of the federal and state constitutions and state law. Funds assessed under the QAF are made available, in part, to enhance federal financial participation in the Medi-Cal program. Plaintiffs seek a refund of fees paid. The trial court ruled the QAF is properly characterized as a “tax” rather than a “fee.” Trial then proceeded on plaintiffs’ claims for refund of QAF amounts paid as an allegedly illegal and improperly collected tax. The QAF amounts collected from all providers to date total nearly \$2 billion, and California has received additional federal financial participation based on its imposition and collection of the QAF. An adverse ruling could negatively affect the state’s receipt of federal funds. The trial court ruled for the state, finding that the QAF is constitutionally valid. Plaintiffs appealed (Court of Appeal, Third Appellate District, Case No. C070361).

A series of federal court cases challenging state legislation requiring reductions in Medi-Cal reimbursements (under AB 5 and AB 1183) were argued before the United States Supreme Court in 2011 and remanded to the Ninth Circuit Court of Appeal, where they remain in mediation. *Independent Living Center of Southern California, et al. v. Shewry, et al.* (U.S. District Court, Central District, Case No. CV 08-3315 CAS (MANx)) (AB 5 reductions for various Medi-Cal services); *California Pharmacists Association, et al. v. Maxwell-Jolly, et al.* (U.S. District Court, Central District, Case No. CV09-0722) (AB 1183 reductions for doctors, hospitals, pharmacists, and other providers); and *Independent Living Center of Southern California, et al. v. Maxwell-Jolly, et al.* (U.S. District Court, Central District, Case No. CV09-00382) (AB 1183 reductions for prescription drugs). The district court enjoined certain of the reductions and the Ninth Circuit affirmed. (U.S. Court of Appeals, Ninth Circuit, Case No. 08-56422.) After the United States Supreme Court heard argument but before it decided the cases, DHCS reached an agreement with the federal government under which DHCS withdrew most of its pending requests for approvals of the reductions (referred to as State Plan Amendments (“SPAs”)) for the period in which the reductions had been enjoined and received approval for the SPAs for the periods for which reductions had not been enjoined. The United States Supreme

Court (United States Supreme Court, Case No. 09-958) vacated the judgment and remanded the matters to the Ninth Circuit for further review in light of the federal government's intervening action approving the state's plan to implement the rate reductions. The parties are currently mediating their remaining claims regarding the reductions.

In *California Medical Association, et al. v. Shewry, et al.* (Los Angeles County Superior Court, Case No. BC 390126), professional associations representing Medi-Cal providers seek to enjoin implementation of the 10 percent Medi-Cal rate reductions that were to go into effect on July 1, 2008, alleging that the legislation violates federal Medicaid requirements, state laws and regulations, and the state Constitution. The trial court denied plaintiffs' motion for a preliminary injunction. Plaintiffs filed an appeal, which was dismissed at their request. (Court of Appeal, Second Appellate District, Case No. B210440.) Plaintiffs have indicated that they will file an amended petition seeking the retrospective relief the Ninth Circuit awarded in the *Independent Living Center* case, discussed above, after final disposition of that case. The matter is stayed pending final resolution in the *Independent Living Center* matter. A final decision adverse to the state in this matter could result in costs to the General Fund of \$508.2 million.

In *California Pharmacists Association, et al. v. Maxwell-Jolly, et al.* (U.S. District Court, Central District, Case No. CV09-08200), Medi-Cal pharmacy providers filed a suit challenging reimbursement rates, including the use by DHCS of reduced published average wholesale price data to establish reimbursement rates, and challenging the Legislature's amendment of Welfare and Institutions Code section 14105.45 and enactment of Welfare and Institutions Code section 14105.455. Plaintiffs seek injunctive relief based on alleged violations of federal law. The district court granted a request for preliminary injunction in part, with respect to sections 14104.45 and 14105.455, and denied it in part, with respect to the use of reduced published average wholesale price data to establish reimbursement rates. Plaintiffs filed a motion seeking to modify the district court ruling, and both parties filed notices of appeal to the Ninth Circuit Court of Appeals. The parties have requested mediation. At this time it is unknown what fiscal impact this case would have on the state's General Fund.

In *Centinela Freeman Emergency Medical Associates, et al. v. Maxwell-Jolly, et al.* (Los Angeles County Superior Court, Case No. BC 406372), filed as a class action on behalf of emergency room physicians and emergency department groups, plaintiffs claim that Medi-Cal rates for emergency room physicians are below the cost of providing care. The trial court granted the petition of the plaintiffs and ordered DHCS to conduct an annual review of reimbursement rates for physicians and dentists pursuant to Welfare and Institutions Code section 14079. A final decision in this matter adverse to the state could result in costs to the General Fund of \$250 million.

In *Sierra Medical Services Alliance, et al. v. Maxwell-Jolly, et al.* (U.S. District Court, Central District, Case No. CV10-04182), emergency medical transportation companies challenge California regulations that set Medi-Cal reimbursement rates paid for medical transportation services. Plaintiffs seek damages and injunctive relief, alleging constitutional violations. At this time it is unknown what fiscal impact this case would have on the state's General Fund.

In *California Hospital Association v. Maxwell-Jolly, et al.* (Sacramento County Superior Court, Case No. 34-2010-80000673), plaintiff challenges limits on Medi-Cal reimbursement

rates for hospital services enacted in 2008, and which were to take effect October 1, 2008 or March 1, 2009, as allegedly violating federal law. Plaintiff seeks to enjoin the implementation of the limits. This matter is currently stayed. At this time it is unknown what fiscal impact this matter may have on the state's General Fund.

Medicaid providers and beneficiaries filed four law suits against both the State and the federal government, seeking to enjoin a set of rate reductions (the AB 97 reductions) that were approved by the federal government in October 2011 with an effective date of June 1, 2011. *Managed Pharmacy Care, et al., v. Sebelius* (U.S. District Court, Central District, Case No. 2:11-cv-09211-CAS(MANx)); *California Medical Assoc., et al., v. Douglas* (U.S. District Court, Central District, Case, No. 2:11-cv-09688-CAS (MANx)); *California Medical Transportation Assoc. Inc., v. Douglas* (U.S. District Court, Central District, Case No. 2:11-cv-09830-CAS (MANx)); *California Hospital Association, et al., v. Douglas* (U.S. District Court, Central District, Case No. CV-11-09078 CAS (MRWx)). The Medicaid rates at issue in the four cases include pharmacy service and prescription drugs; services provided by skilled nursing facilities that are distinct part units within a hospital; non-emergency medical transportation services; physician services; dental services; durable medical equipment; and emergency ambulance services. The district court entered a series of preliminary injunctions to prevent the rate reductions from taking effect. Both the federal and state government (DHCS) appealed to the Ninth Circuit Court of Appeals. The Ninth Circuit reversed the district court, vacated the preliminary injunctions, and remanded the case. The Ninth Circuit denied plaintiffs' petitions for rehearing and request for a stay. The United States Supreme Court denied plaintiffs' petitions for certiorari.

Prison Healthcare Reform and Reduction of Prison Population

The adult prison health care delivery system includes medical health care, mental health care and dental health care. There are two significant cases pending in federal district courts challenging the constitutionality of prison health care. *Plata v. Brown* (U.S. District Court, Northern District, Case No. C 01-1351 TEH) is a class action regarding the adequacy of medical health care; and *Coleman v. Brown* (U.S. District Court, Eastern District, Case No. CIV S-90-0520 LKK JFM P) is a class action regarding mental health care. A third case, *Armstrong v. Brown* (U.S. District Court, Northern District, Case No. C 94-02307 CW) is a class action on behalf of inmates with disabilities alleging violations of the Americans with Disabilities Act and Section 504 of the Rehabilitation Act. In *Plata* the district court appointed a Receiver, who took office in April 2006, to run and operate the medical health care portion of the health care delivery system. The *Plata* Receiver and the Special Master appointed by the *Coleman* court, joined by the court representative appointed by the *Armstrong* court, meet routinely to coordinate efforts in these cases. To date, ongoing costs of remedial activities have been incorporated into the state's budget process. However, at this time, it is unknown what future financial impact this litigation may have on the state's General Fund.

In *Plata* and *Coleman*, discussed above, a three-judge panel was convened to consider plaintiffs' motion for a prisoner-release order. The motions alleged that prison overcrowding was the primary cause of unconstitutional medical and mental health care. After a trial, the panel issued a prisoner release order and ordered the state to prepare a plan for the reduction of approximately 40,000 prisoners over two years. The state filed its prisoner-reduction plan with

the three-judge panel and filed an appeal in the United States Supreme Court. The United States Supreme Court affirmed the prisoner release order.

On January 7, 2013, the state moved to terminate the *Coleman* matter arguing that the prison mental health-care system is constitutional. The district court denied the state's motion and the state appealed to the Ninth Circuit. In January 2013, the state also moved to vacate the three-judge panel's prisoner-release order arguing that further population reductions are unnecessary in order for the state to provide appropriate health care to the prison population. The three-judge panel denied the state's motion and ordered the state to meet the court-ordered reduction by December 31, 2013. The state requested a stay of the order, which was denied by the United States Supreme Court. The state's request for review of the court-ordered reduction was also denied by the United States Supreme Court. Based on enactment of SB 105, which appropriated \$315 million for a mix of increased prison capacity and long-term reforms to control prison crowding, the state asked the three-judge panel for a three-year extension of the deadline for compliance with the population cap. On February 10, 2014, the three-judge panel issued its order granting the state a two-year extension to meet the final population-reduction benchmark. The order requires the state to comply in part through a combination of additional in-state capacity in county jails, community correctional facilities, and a private prison, and through newly enacted programs, including the development of additional measures regarding reforms to state penal and sentencing laws designed to reduce the prison population. The three-judge panel will also appoint a "compliance officer" to bring the state into compliance if any benchmark is missed by ordering the release of inmates.

Actions Regarding Proposed Sale of State-Owned Properties

Two taxpayers filed a lawsuit seeking to enjoin the sale of state-owned office properties, which was originally scheduled to close in December 2010, on the grounds that the sale of certain of the buildings that house appellate court facilities required the approval of the Judicial Council, which had not been obtained, and that the entire sale constituted a gift of public funds in violation of the state Constitution and a waste of public funds in violation of state law. *Epstein, et al. v. Schwarzenegger, et al.* (San Francisco County Superior Court, Case. No. CGC-10-505436). Plaintiffs' request for a preliminary injunction was denied. In a second action filed after the state decided not to proceed with the sale, and now coordinated with the *Epstein* matter, the prospective purchaser seeks to compel the state to proceed with the sale of the state-owned properties, or alternatively, for damages for breach of contract. *California First, LP v. California Department of General Services, et al.* (Los Angeles County Superior Court, Case No. BC457070). The trial court denied the state's motion for judgment on the pleadings, in which the state asserted that the plaintiff should not be permitted to pursue claims for damages. The parties have stipulated to bifurcate the matters for trial and to stay the *Epstein* matter pending trial of the *California First* matter.

High-Speed Rail Litigation

In *Tos, et al. v. California High-Speed Rail Authority, et al.* (Sacramento County Superior Court, Case No. 34-2011-00113919), petitioners claim that the Authority has not complied with the state high-speed rail bond act in approving plans for the high-speed rail system. The trial court ruled that the Authority's plan for funding the high-speed rail project did not comply with

certain requirements in the bond act, and ordered the Authority to rescind the plan. Respondents' motion for judgment on the pleadings on petitioners' remaining claims was denied by the trial court on March 4, 2014. *On March 7, the trial court stayed further proceedings in Tos to permit the state to seek review of the ruling.* In *High-Speed Rail Authority, et al. v. All Persons Interested, etc.* (Sacramento County Superior Court, Case No. 34-2013-00140689), the Authority is seeking to validate issuance of the bonds authorized under the bond act for high-speed rail system. The trial court denied validation of the bonds. Respondents in *Tos* and plaintiffs in the validation action filed a petition in the California Supreme Court from the judgment in the validation action and the order in *Tos* requiring the Authority to rescind the funding plan, and the Supreme Court transferred the proceeding to the court of appeal (Court of Appeal, Third Appellate District, Case No. C075668). On February 14, 2014, the court of appeal granted an alternative writ and stayed the trial court's order in *Tos* directing the Authority to rescind the funding plan. Briefing is to be concluded by April 1, 2014. In the event of a ruling adverse to the state in these pending matters that delays or prevents issuance of the bonds, it is possible that the federal government may require the state to reimburse federal funds provided for the high-speed rail project. The potential amount of any such reimbursement cannot be determined at this time.

BANK ARRANGEMENTS

The table immediately following the text of APPENDIX A, prior to the State Debt Tables, includes certain information relating to bank arrangements the state has entered into. See also "STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Capital Facilities Financing – Bank Arrangements."

STATE DEBT TABLES

The tables which follow provide information on outstanding state debt, authorized but unissued general obligation bonds and commercial paper notes, debt service requirements for state general obligation and lease-revenue bonds, and authorized and outstanding state revenue bonds. The table titled "Bank Arrangements" contains certain information relating to letters of credit, liquidity facilities and other bank arrangements in connection with variable rate obligations and commercial paper notes. Also, see "STATE INDEBTEDNESS AND OTHER OBLIGATIONS." For purposes of these tables, "General Fund bonds," also known as "non-self liquidating bonds," are general obligation bonds expected to be paid from the General Fund without reimbursement from any other fund. Although the principal of general obligation commercial paper notes in the "non-self liquidating" category is legally payable from the General Fund, the state expects that principal of such commercial paper notes will be paid only from the issuance of new commercial paper notes or the issuance of long-term general obligation bonds to retire the commercial paper notes. Interest on "non-self liquidating" general obligation commercial paper notes is payable from the General Fund.

"Enterprise Fund bonds," also known as "self liquidating bonds," are general obligation bonds for which program revenues are expected to be sufficient to reimburse in full the General Fund for debt service payments, but any failure to make such a reimbursement does not affect the obligation of the state to pay principal and interest on the bonds from the General Fund.

“Special Revenue Fund bonds” also known as Economic Recovery Bonds or ERBs, are “self liquidating” general obligation bonds which are primarily secured by a pledge of a one-quarter cent statewide sales and use tax deposited in the Fiscal Recovery Fund. Debt service payments are made directly from the Fiscal Recovery Fund and not the General Fund. The Special Revenue Fund bonds are also general obligations of the state to which the full faith and credit of the state are pledged to the punctual payment of the principal of and interest thereon, if the sales tax revenues are insufficient.

As of March 3, 2014, there was \$892,325,000 principal amount of commercial paper notes outstanding.

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BANK ARRANGEMENTS TABLE

(See “STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Capital Facilities Financing – Bank Arrangements.”)

As of February 1, 2014

<u>Program</u>	<u>Series</u>	<u>Outstanding Par Amount^(a)</u>	<u>Credit Provider</u>	<u>Expiration</u>	<u>Type of Credit</u>	<u>Reset Mode</u>
GO VRDOs	2003A 1	\$50,000,000	JPMorgan Chase Bank	12/16/2016	LOC	Daily
	2003A 2-3	\$200,000,000	Bank of Montreal	10/16/2015	LOC	Daily
GO VRDOs	2003B 1-4	\$250,000,000	JPMorgan Chase (80.0%)	11/10/2016	LOC	Weekly
			CA Public Employees' Retirement System (20.0%)			
GO VRDOs	2003C 1	\$100,000,000	Bank of America, N.A.	12/16/2016	LOC	Weekly
	2003C 3-4	\$100,000,000	U.S. Bank National Association	04/12/2017	LOC	Weekly
GO VRDOs	2004A 1, 4 & 5	\$200,000,000	Citibank, N.A.	10/15/2015	LOC	Daily
GO VRDOs	2004A 2 & 3	\$150,000,000	State Street Bank and Trust Company	11/10/2016	LOC	Daily
GO VRDOs	2004A 6, 7, 8 & 10	\$200,000,000	Citibank, N.A.	10/15/2015	LOC	Weekly
GO VRDOs	2004A 9	\$50,000,000	State Street Bank and Trust Company	11/10/2016	LOC	Weekly
GO VRDOs	2004B 1-3	\$165,000,000	Citibank, N.A.	10/15/2015	LOC	Daily
GO VRDOs	2004B 4	\$35,000,000	Citibank, N.A.	10/15/2015	LOC	Weekly
GO VRDOs	2004B 5-6	\$100,000,000	U.S. Bank National Association	04/06/2015	LOC	Weekly
GO VRDOs	2005A-1-1	\$85,850,000	Royal Bank of Canada	11/04/2016	LOC	Weekly
GO VRDOs	2005A-1-2	\$85,750,000	Royal Bank of Canada	11/04/2016	LOC	Weekly
GO VRDOs	2005A-2-1	\$143,200,000	Barclays Bank PLC	04/11/2017	LOC	Weekly
GO VRDOs	2005A-2-2	\$28,400,000	Royal Bank of Canada	11/04/2016	LOC	Weekly
GO VRDOs	2005A-3	\$49,100,000	Bank of America, N.A.	11/10/2016	LOC	Weekly
GO VRDOs	2005B-1	\$147,100,000	Bank of America, N.A.	02/17/2017	LOC	Weekly
GO VRDOs	2005B-2	\$98,100,000	Bank of Tokyo – Mitsubishi UFJ, Ltd.	11/10/2016	LOC	Weekly
GO VRDOs	2005B-3	\$49,100,000	Barclays Bank PLC	04/11/2017	LOC	Weekly
GO VRDOs	2005B-4	\$49,100,000	JPMorgan Chase Bank	12/16/2016	LOC	Weekly
GO VRDOs	2005B-5	\$88,890,000	Barclays Bank PLC	04/11/2017	LOC	Weekly

<u>Program</u>	<u>Series</u>	<u>Outstanding Par Amount^(a)</u>	<u>Credit Provider</u>	<u>Expiration</u>	<u>Type of Credit</u>	<u>Reset Mode</u>
GO VRDOs	2005B-7	\$49,100,000	JPMorgan Chase Bank	12/16/2016	LOC	Daily
Total GO VRDOs		\$2,473,690,000				
ERB VRDOs	2004C-4	\$110,370,000	JPMorgan Chase Bank	06/13/2014	LOC	Daily
Total ERB VRDOs		\$110,370,000				
GO CP ^(a)	A1/B1	\$500,000,000	Wells Fargo Bank, N.A.	12/17/2017	LOC	Up to 90 days
	A2/B2	\$500,000,000	Royal Bank of Canada	12/16/2016	LOC	Up to 90 days
	A3/B3	\$200,000,000	JPMorgan Chase Bank (75)	12/16/2016		
			CA Public Employees' Retirement System (25%)		LOC	Up to 90 days
	A4/B4	\$150,000,000	Morgan Stanley Bank, N.A.	12/16/2016	LOC	Up to 90 days
	A5/B5	\$125,000,000	U.S. Bank National Association	12/16/2016	LOC	Up to 90 days
	A6/B6	\$50,000,000	Bank of America, N.A.	12/16/2016	LOC	Up to 90 days
	A7/B7	\$125,000,000	Mizuho Bank, Ltd.	12/19/2016	LOC	Up to 90 days
	A8/B8	\$75,000,000	Bank of the West	02/17/2017	LOC	Up to 90 days
Total CP		\$1,725,000,000				
Total Par		\$4,309,060,000				

^(a) For commercial paper (CP), the total outstanding par represents the maximum principal commitment under the related LOC.
Source: State Treasurer's Office.

OUTSTANDING STATE DEBT
FISCAL YEARS 2008-09 THROUGH 2012-13
(Dollars in Thousands Except for Per Capita Information)

	<u>2008-09</u>	<u>2009-10</u>	<u>2010-11</u>	<u>2011-12</u>	<u>2012-13</u>
Outstanding Debt (a)					
General Obligation Bonds					
General Fund (Non-Self Liquidating).....	\$ 59,037,759	\$ 68,766,304	\$ 71,283,705	\$ 73,060,865	\$ 74,456,230
Enterprise Fund (Self Liquidating).....	\$ 1,655,265	\$ 1,475,440	\$ 1,216,115	\$ 1,115,935	\$ 884,180
Special Revenue Fund (Self Liquidating).....	\$ 8,223,450	\$ 7,720,220	\$ 6,787,220	\$ 5,910,480	\$ 4,731,745
Total General Obligation Bonds.....	<u>\$ 68,916,474</u>	<u>\$ 77,961,964</u>	<u>\$ 79,287,040</u>	<u>\$ 80,087,280</u>	<u>\$ 80,072,155</u>
Revenue Bonds					
Lease-Purchase Debt.....	\$ 8,051,007	\$ 9,887,600	\$ 9,426,325	\$ 11,330,355	\$ 11,822,140
Proposition 1A Receivables Program.....	N/A	\$ 1,895,000	\$ 1,895,000	\$ 1,895,000	\$ 0
Total Revenue Bonds.....	<u>\$ 8,051,007</u>	<u>\$ 11,782,600</u>	<u>\$ 11,321,325</u>	<u>\$ 13,225,355</u>	<u>\$ 11,822,140</u>
Total Outstanding General Obligation and Revenue Bonds.....	<u>\$ 76,967,481</u>	<u>\$ 89,744,564</u>	<u>\$ 90,608,365</u>	<u>\$ 93,312,635</u>	<u>\$ 91,894,295</u>
Bond Sales During Fiscal Year					
Non-Self Liquidating General Obligation Bonds....	\$ 13,934,985	\$ 12,446,005	\$ 4,525,000	\$ 7,817,390	\$ 7,417,170
Self Liquidating General Obligation Bonds.....	\$ 0	\$ 118,710	\$ 0	\$ 0	\$ 0
Proposition 1A Receivables Revenue Bonds.....	N/A	\$ 1,895,000	\$ 0	\$ 0	\$ 0
Self Liquidating Special Fund Revenue Bonds.....	\$ 0	\$ 3,435,615	\$ 0	\$ 438,635	\$ 0
Lease-Purchase Debt.....	\$ 641,975	\$ 2,269,235	\$ 0	\$ 2,627,115	\$ 1,678,130
Debt Service (b)					
Non-Self Liquidating General Obligation Bonds....	\$ 4,021,605	\$ 5,035,363	\$ 5,704,729	\$ 5,782,240	\$ 5,424,867
Lease-Purchase Debt.....	\$ 825,788	\$ 881,994	\$ 973,824	\$ 980,862	\$ 1,209,353
General Fund Receipts (c).....	\$ 87,774,952	\$ 88,654,941	\$ 95,536,379	\$ 87,769,787	\$ 103,424,674
Non-Self Liquidating General Obligation Bonds					
Debt Service as a Percentage of General Fund Receipts.....	4.58%	5.68%	5.97%	6.59%	5.25%
Lease-Purchase Debt Service as a Percentage of General Fund Receipts.....	0.94	0.99%	1.02%	1.12%	1.17%
Population (d).....	36,856,222	37,077,204	37,309,382	37,570,366	37,832,036
Non-Self Liquidating General Obligation Bonds					
Outstanding per Capita.....	\$ 1,601.84	\$ 1,854.68	\$ 1,910.61	\$ 1,944.64	\$ 1,968.07
Lease-Purchase Debt Outstanding per Capita.....	\$ 218.44	\$ 266.68	\$ 252.65	\$ 301.58	\$ 312.49
Personal Income (e).....	\$ 1,610,698,000	\$ 1,516,677,000	\$ 1,564,209,000	\$ 1,645,138,000	\$ 1,720,052,000
Non-Self Liquidating General Obligation Bonds					
Outstanding as Percentage of Personal Income.....	3.67%	4.53%	4.56%	4.44%	4.33%
Lease-Purchase Debt Outstanding as Percentage of Personal Income.....	0.50%	0.65%	0.60%	0.69%	0.69

- (a) Principal outstanding as of July 1 of the next fiscal year. Includes the initial value of capital appreciation bonds rather than the accreted value.
- (b) Calculated on a cash basis. The amounts do not reflect any interest subsidy under the Build America Bonds program. Subsidy not pledged to the repayment of debt service. Debt service costs of bonds issued in any fiscal year largely appear in subsequent fiscal years.
- (c) Calculated on a cash basis. General Fund Receipts includes both revenues and nonrevenues, such as borrowings, the proceeds of which are deposited in the General Fund (e.g. tobacco securitization bonds and economic recovery bonds).
- (d) As of July 1, the beginning of the fiscal year.
- (e) Revised estimates as of June 28, 2013.

SOURCES: Population: State of California, Department of Finance.

Personal Income: United States, Department of Commerce, Bureau of Economic Analysis

Outstanding Debt, Bonds Sales During Fiscal Year and Debt Service: State of California, Office of the Treasurer.

General Fund Receipts: State of California, Office of the State Controller.

AUTHORIZED AND OUTSTANDING GENERAL OBLIGATION BONDS
As of February 1, 2014
(Thousands)

	Voter Authorization Date	Authorization Amount \$	Long Term Bonds Outstanding \$	Commercial Paper Outstanding (a) \$	Unissued \$
GENERAL FUND BONDS (Non-Self Liquidating)					
+ 1988 School Facilities Bond Act	11/08/88	797,745	44,140	0	0
+ 1990 School Facilities Bond Act	06/05/90	797,875	105,135	0	0
+ 1992 School Facilities Bond Act	11/03/92	898,211	293,080	0	0
California Clean Water, Clean Air, Safe Neighborhood Parks, and Coastal Protection Act of 2002	03/05/02	2,600,000	2,207,535	0	259,240
+ California Library Construction and Renovation Bond Act of 1988	11/08/88	72,405	14,010	0	0
*+ California Park and Recreational Facilities Act of 1984	06/05/84	368,900	13,925	0	0
* California Parklands Act of 1980	11/04/80	285,000	2,960	0	0
California Reading and Literacy Improvement and Public Library Construction and Renovation Bond Act of 2000	03/07/00	350,000	279,335	0	5,040
*+ California Safe Drinking Water Bond Law of 1976	06/08/76	172,500	3,315	0	0
* California Safe Drinking Water Bond Law of 1984	11/06/84	75,000	2,080	0	0
* California Safe Drinking Water Bond Law of 1986	11/04/86	100,000	25,490	0	0
California Safe Drinking Water Bond Law of 1988	11/08/88	75,000	29,945	0	0
*+ California Wildlife, Coastal, and Park Land Conservation Act	06/07/88	768,670	129,085	0	0
Children's Hospital Bond Act of 2004	11/02/04	750,000	664,410	0	47,445
Children's Hospital Bond Act of 2008	11/04/08	980,000	528,865	36,350	412,890
Class Size Reduction Kindergarten-University Public Education Facilities Bond Act of 1998 (Hi-Ed)	11/03/98	2,500,000	1,806,515	0	0
Class Size Reduction Kindergarten-University Public Education Facilities Bond Act of 1998 (K-12)	11/03/98	6,700,000	4,283,905	0	11,400
Clean Air and Transportation Improvement Bond Act of 1990	06/05/90	1,990,000	855,430	0	17,570
* Clean Water Bond Law of 1984	11/06/84	325,000	12,290	0	0
* Clean Water and Water Conservation Bond Law of 1978	06/06/78	375,000	4,985	0	0
Clean Water and Water Reclamation Bond Law of 1988	11/08/88	65,000	21,970	0	0
* Community Parklands Act of 1986	06/03/86	100,000	3,135	0	0
* County Correctional Facility Capital Expenditure Bond Act of 1986	06/03/86	495,000	17,810	0	0
County Correctional Facility Capital Expenditure and Youth Facility Bond Act of 1988	11/08/88	500,000	79,935	0	0
Disaster Preparedness and Flood Prevention Bond Act of 2006	11/07/06	4,090,000	2,244,880	0	1,818,652

AUTHORIZED AND OUTSTANDING GENERAL OBLIGATION BONDS

As of February 1, 2014

(Thousands)

	Voter Authorization Date	Authorization Amount \$	Long Term Bonds Outstanding \$	Commercial Paper Outstanding (a) \$	Unissued \$
GENERAL FUND BONDS (Non-Self Liquidating)					
Earthquake Safety and Public Buildings Rehabilitation Bond Act of 1990	06/05/90	300,000	93,605	0	9,765
* Fish and Wildlife Habitat Enhancement Act of 1984	06/05/84	85,000	5,455	0	0
Higher Education Facilities Bond Act of 1988	11/08/88	600,000	26,090	0	0
Higher Education Facilities Bond Act of June 1990	06/05/90	450,000	53,185	0	540
Higher Education Facilities Bond Act of June 1992	06/02/92	900,000	350,695	0	0
Highway Safety, Traffic Reduction, Air Quality, and Port Security Bond Act of 2006	11/07/06	19,925,000	12,213,600	457,630	6,997,140
Housing and Emergency Shelter Trust Fund Act of 2002	11/05/02	2,100,000	1,326,045	0	132,535
Housing and Emergency Shelter Trust Fund Act of 2006	11/07/06	2,850,000	1,528,620	0	1,258,990
Housing and Homeless Bond Act of 1990	06/05/90	150,000	1,755	0	0
Kindergarten-University Public Education Facilities Bond Act of 2002 (Hi-Ed)	11/05/02	1,650,000	1,460,155	0	0
Kindergarten-University Public Education Facilities Bond Act of 2002 (K-12)	11/05/02	11,400,000	9,464,830	0	61,840
Kindergarten-University Public Education Facilities Bond Act of 2004 (Hi-Ed)	03/02/04	2,300,000	2,094,390	0	62,869
Kindergarten-University Public Education Facilities Bond Act of 2004 (K-12)	03/02/04	10,000,000	9,004,090	32,660	184,590
Kindergarten-University Public Education Facilities Bond Act of 2006 (Hi-Ed)	11/07/06	3,087,000	2,935,525	3,255	112,205
Kindergarten-University Public Education Facilities Bond Act of 2006 (K-12)	11/07/06	7,329,000	6,282,905	3,025	990,535
* Lake Tahoe Acquisitions Bond Act	08/02/82	85,000	300	0	0
* New Prison Construction Bond Act of 1986	11/04/86	500,000	4,895	0	0
New Prison Construction Bond Act of 1988	11/08/88	817,000	21,080	0	2,165
New Prison Construction Bond Act of 1990	06/05/90	450,000	26,065	0	605
Passenger Rail and Clean Air Bond Act of 1990	06/05/90	1,000,000	59,225	0	0
Public Education Facilities Bond Act of 1996 (Higher Education)	03/26/96	975,000	543,095	3,600	10,880
++ Public Education Facilities Bond Act of 1996 (K-12)	03/26/96	2,012,035	1,008,925	0	0
Safe Drinking Water, Clean Water, Watershed Protection, and Flood Protection Act	03/07/00	1,970,000	1,488,825	0	129,346
Safe Drinking Water, Water Quality and Supply, Flood Control, River and Coastal Protection Bond Act of 2006	11/07/06	5,388,000	2,398,550	0	2,957,710
Safe Neighborhood Parks, Clean Water, Clean Air, and Coastal Protection Bond Act of 2000	03/07/00	2,100,000	1,572,485	0	73,820
Safe, Clean, Reliable Water Supply Act	11/05/96	995,000	634,825	0	89,070
Safe, Reliable High-Speed Passenger Train Bond Act for the 21st Century	11/04/08	9,950,000	623,705	0	9,244,480
* School Building and Earthquake Bond Act of 1974	11/05/74	40,000	17,305	0	0

AUTHORIZED AND OUTSTANDING GENERAL OBLIGATION BONDS
As of February 1, 2014
(Thousands)

	Voter Authorization Date	Authorization Amount \$	Long Term Bonds Outstanding \$	Commercial Paper Outstanding (a) \$	Unissued \$
GENERAL FUND BONDS (Non-Self Liquidating)					
School Facilities Bond Act of 1990	11/06/90	800,000	166,010	0	0
School Facilities Bond Act of 1992	06/02/92	1,900,000	602,880	0	10,280
Seismic Retrofit Bond Act of 1996	03/26/96	2,000,000	1,239,490	0	0
* State, Urban, and Coastal Park Bond Act of 1976	11/02/76	280,000	4,355	0	0
Stem Cell Research and Cures Bond Act of 2004	11/02/04	3,000,000	1,292,415	133,610	1,516,475
Veterans Homes Bond Act of 2000	03/07/00	50,000	35,205	0	975
Voting Modernization Bond Act of 2002	03/05/02	200,000	52,035	0	64,495
Water Conservation Bond Law of 1988	11/08/88	60,000	24,245	0	5,235
* Water Conservation and Water Quality Bond Law of 1986	06/03/86	150,000	35,330	0	13,730
Water Security, Clean Drinking Water, Coastal and Beach Protection Act of 2002	11/05/02	3,440,000	2,820,495	1,810	404,574
Total General Fund Bonds		127,519,341	75,186,850	671,940	26,907,086
ENTERPRISE FUND BONDS (Self Liquidating)					
* California Water Resources Development Bond Act	11/08/60	1,750,000	266,535	0	167,600
Veterans Bond Act of 1986	06/03/86	850,000	58,590	0	0
Veterans Bond Act of 1988	06/07/88	510,000	37,290	0	0
Veterans Bond Act of 1990	11/06/90	400,000	50,875	0	0
Veterans Bond Act of 1996	11/05/96	400,000	159,040	0	0
Veterans Bond Act of 2000	11/07/00	500,000	178,595	0	238,610
+++ Veterans Bond Act of 2008	11/04/08	300,000	0	0	300,000
Total Enterprise Fund Bonds		4,710,000	750,925	0	706,210

AUTHORIZED AND OUTSTANDING GENERAL OBLIGATION BONDS
As of February 1, 2014
(Thousands)

	Voter Authorization Date	Authorization Amount \$	Long Term Bonds Outstanding \$	Commercial Paper Outstanding (a) \$	Unissued \$
SPECIAL REVENUE FUND BONDS (Self Liquidating)					
* Economic Recovery Bond Act	04/10/04	15,000,000	4,581,745	0	0
Total Special Revenue Fund Bonds		<u>15,000,000</u>	<u>4,581,745</u>	<u>0</u>	<u>0</u>
TOTAL GENERAL OBLIGATION BONDS		<u>147,229,341</u>	<u>80,519,520</u>	<u>671,940</u>	<u>27,613,296</u>

(a) A total of not more than \$1.649 billion of commercial paper principal plus accrued interest may be owing at one time. Bond acts marked with an asterisk (*) are not legally permitted to utilize commercial paper.

+ SB 1018 (06/27/2012) reduced the voter authorized amount
++ SB 71 (06/27/2013) reduced the voter authorized amount
+++ AB 639 (10/10/2013) reduced the voter authorized amount

SOURCE: State of California, Office of the Treasurer.

**GENERAL OBLIGATION AND REVENUE BONDS
SUMMARY OF DEBT SERVICE REQUIREMENTS
As of February 1, 2014**

	Total Debt		
	Interest	Principal	Total (a)
GENERAL OBLIGATION BONDS			
<u>GENERAL FUND NON-SELF LIQUIDATING (b)</u>			
Fixed Rate	\$ 62,174,844,733.08	\$ 71,765,060,000.00	\$ 133,939,904,733.08
Variable Rate (c)	301,550,425.05	3,421,790,000.00	3,723,340,425.05
<u>ENTERPRISE FUND SELF LIQUIDATING</u>			
Fixed Rate	367,142,386.25	750,925,000.00	1,118,067,386.25
<u>SPECIAL REVENUE FUND SELF LIQUIDATING (d)</u>			
Fixed Rate	925,123,071.25	3,971,375,000.00	4,896,498,071.25
Variable Rate (e)	119,239,604.99	610,370,000.00	729,609,604.99
REVENUE BONDS			
<u>GENERAL FUND LEASE-REVENUE</u>			
Lease-Revenue	6,016,372,794.84	10,235,955,000.00	16,252,327,794.84
General Fund and Lease-Revenue Total (f)	\$ 69,904,273,015.46	\$ 90,755,475,000.00	\$ 160,659,748,015.46

(a) Includes scheduled mandatory sinking fund payments.

(b) Does not include outstanding commercial paper.

(c) The estimate of future interest payments is based on rates in effect as of February 1, 2014. The interest rates for the daily, weekly and monthly rate bonds range from 0.02 - 1.19 .

The Highway Safety, Traffic Reduction, Air Quality, and Port Security Bond Act of 2006, Series 2013A & 2013B currently bear interest at a fixed rate of 4.00% until reset date, and are assumed to bear that rate from reset until maturity.

(d) Economic Recovery Bonds.

(e) The estimate of future interest payments is based on the rate in effect as of February 1, 2014 which is 0.04 .

\$500,000,000 of the Series 2009B Economic Recovery Bonds bear interest at fixed rates ranging from 3.50 - 5.00% until reset date, and are assumed to bear interest at the rate of 4.00% from each reset date to maturity.

(f) Estimated interest included.

SOURCE: State of California, Office of the Treasurer.

**SCHEDULE OF DEBT SERVICE REQUIREMENTS
FOR GENERAL FUND NON-SELF LIQUIDATING BONDS**

Fixed Rate

As of February 1, 2014

Fiscal Year Ending June 30	Current Debt		
	Interest (a)	Principal	Total (b)
2014	\$ 1,689,522,604.83	\$ 1,150,480,000.00	\$ 2,840,002,604.83 (c)
2015	3,832,282,670.10	2,634,720,000.00	6,467,002,670.10
2016	3,713,079,237.60	2,720,595,000.00	6,433,674,237.60
2017	3,593,940,079.37	2,380,300,000.00	5,974,240,079.37
2018	3,483,876,992.45	2,289,465,000.00	5,773,341,992.45
2019	3,369,814,205.62	2,403,105,000.00	5,772,919,205.62
2020	3,229,001,282.64	2,609,340,000.00	5,838,341,282.64
2021	3,110,212,697.73	2,185,485,000.00	5,295,697,697.73
2022	2,992,796,090.31	2,489,435,000.00	5,482,231,090.31
2023	2,874,073,701.78	2,073,530,000.00	4,947,603,701.78
2024	2,774,560,144.18	1,785,305,000.00	4,559,865,144.18
2025	2,684,163,938.15	1,950,170,000.00	4,634,333,938.15
2026	2,580,664,257.85	2,118,670,000.00	4,699,334,257.85
2027	2,469,084,593.31	2,243,690,000.00	4,712,774,593.31
2028	2,358,583,230.86	2,289,355,000.00	4,647,938,230.86
2029	2,248,238,237.60	2,298,305,000.00	4,546,543,237.60
2030	2,130,605,109.31	2,607,880,000.00	4,738,485,109.31
2031	1,989,642,783.11	2,685,900,000.00	4,675,542,783.11
2032	1,861,760,909.40	2,482,680,000.00	4,344,440,909.40
2033	1,728,773,407.51	2,543,930,000.00	4,272,703,407.51
2034	1,600,016,328.50	3,424,105,000.00	5,024,121,328.50
2035	1,363,823,699.85	3,170,320,000.00	4,534,143,699.85
2036	1,173,535,550.76	2,782,530,000.00	3,956,065,550.76
2037	999,520,824.37	3,122,660,000.00	4,122,180,824.37
2038	815,468,859.44	3,068,625,000.00	3,884,093,859.44
2039	667,494,728.95	3,415,270,000.00	4,082,764,728.95
2040	390,870,962.50	1,603,885,000.00	1,994,755,962.50
2041	233,159,093.75	2,190,000,000.00	2,423,159,093.75
2042	130,879,093.75	1,319,000,000.00	1,449,879,093.75
2043	75,421,718.75	1,326,325,000.00	1,401,746,718.75
2044	9,977,698.75	400,000,000.00	409,977,698.75
Total	\$ 62,174,844,733.08	\$ 71,765,060,000.00	\$ 133,939,904,733.08

(a) The amounts do not reflect any interest subsidy under the Build America Bonds program. Subsidy not pledged to the repayment of debt service.

(b) Includes scheduled mandatory sinking fund payments.
Does not include outstanding commercial paper.

(c) Total represents the remaining debt service requirements from March 1, 2014 through June 30, 2014.

SOURCE: State of California, Office of the Treasurer.

**SCHEDULE OF DEBT SERVICE REQUIREMENTS
FOR GENERAL FUND NON-SELF LIQUIDATING BONDS
Variable Rate
As of February 1, 2014**

Fiscal Year Ending June 30	Current Debt		
	Interest (a)(b)	Principal	Total (c)
2014	\$ 11,882,918.47	\$ -	\$ 11,882,918.47 (d)
2015	22,849,541.12	-	22,849,541.12
2016	22,861,450.23	24,400,000.00	47,261,450.23
2017	22,787,068.27	311,845,000.00	334,632,068.27
2018	22,443,548.48	418,745,000.00	441,188,548.48
2019	21,927,146.48	188,250,000.00	210,177,146.48
2020	21,663,597.42	171,150,000.00	192,813,597.42
2021	21,431,888.01	58,600,000.00	80,031,888.01
2022	21,388,751.75	43,600,000.00	64,988,751.75
2023	21,342,750.41	65,600,000.00	86,942,750.41
2024	21,302,250.37	178,300,000.00	199,602,250.37
2025	21,180,046.46	121,300,000.00	142,480,046.46
2026	21,114,004.79	208,400,000.00	229,514,004.79
2027	16,510,735.75	395,900,000.00	412,410,735.75
2028	7,420,215.60	404,500,000.00	411,920,215.60
2029	2,111,038.47	415,600,000.00	417,711,038.47
2030	811,025.12	173,800,000.00	174,611,025.12
2031	259,318.90	76,700,000.00	76,959,318.90
2032	174,702.64	79,800,000.00	79,974,702.64
2033	85,520.40	82,700,000.00	82,785,520.40
2034	834.99	1,600,000.00	1,600,834.99
2035	350.00	-	350.00
2036	351.52	-	351.52
2037	348.48	-	348.48
2038	350.00	-	350.00
2039	350.00	-	350.00
2040	320.92	1,000,001.00	1,000,321.92
Total	\$ 301,550,425.05	\$ 3,421,790,001.00	\$ 3,723,340,426.05

- (a) The estimate of future interest payments is based on rates in effect as of February 1, 2014. The interest rates for the daily, weekly and monthly rate bonds range from 0.02 - 1.19%.
The Highway Safety, Traffic Reduction, Air Quality, and Port Security Bond Act of 2006, Series 2013A & 2013B currently bear interest at a fixed rate of 4.00% until reset date, and are assumed to bear that rate from reset until maturity.
- (b) The amounts do not reflect any interest subsidy under the Build America Bonds program. Subsidy not pledged to the repayment of debt service.
- (c) Includes scheduled mandatory sinking fund payments.
Does not include outstanding commercial paper.
- (d) Total represents the remaining estimated debt service requirements from March 1, 2014 through June 30, 2014.

SOURCE: State of California, Office of the Treasurer.

**SCHEDULE OF DEBT SERVICE REQUIREMENTS FOR
SPECIAL REVENUE FUND SELF LIQUIDATING BONDS**

Fixed Rate

As of February 1, 2014

Fiscal Year Ending June 30	Current Debt			
	Interest	Principal	Total (a)	
2014	\$ -	\$ -	\$ -	(b)
2015	184,847,398.75	525,615,000.00	710,462,398.75	
2016	157,474,605.00	556,690,000.00	714,164,605.00	
2017	140,025,400.00	165,160,000.00	305,185,400.00	
2018	132,149,376.25	174,290,000.00	306,439,376.25	
2019	113,267,497.50	592,955,000.00	706,222,497.50	
2020	86,361,762.50	496,145,000.00	582,506,762.50	
2021	61,465,062.50	507,445,000.00	568,910,062.50	
2022	36,925,093.75	451,575,000.00	488,500,093.75	
2023	12,571,250.00	500,000,000.00	512,571,250.00	
2024	35,625.00	1,500,000.00	1,535,625.00	
Total	\$ 925,123,071.25	\$ 3,971,375,000.00	\$ 4,896,498,071.25	

(a) Includes scheduled mandatory sinking fund payments.

(b) Total represents the remaining debt service requirements from March 1, 2014 through June 30, 2014.

SOURCE: State of California, Office of the Treasurer.

**SCHEDULE OF DEBT SERVICE REQUIREMENTS FOR
SPECIAL REVENUE FUND SELF LIQUIDATING BONDS**

Variable Rate

As of February 1, 2014

Fiscal Year Ending June 30	Current Debt		
	Interest (a)	Principal	Total (b)
2014	\$ 14,393.46	\$ -	\$ 14,393.46 (c)
2015	21,968,452.05	-	21,968,452.05
2016	20,044,218.72	-	20,044,218.72
2017	20,044,077.28	-	20,044,077.28
2018	20,044,148.00	25,000,000.00	45,044,148.00
2019	18,544,389.91	115,000,000.00	133,544,389.91
2020	12,653,976.81	189,500,000.00	202,153,976.81
2021	4,864,077.28	128,755,000.00	133,619,077.28
2022	968,330.41	66,305,000.00	67,273,330.41
2023	78,047.10	70,035,000.00	70,113,047.10
2024	15,493.97	15,775,000.00	15,790,493.97
Total	\$ 119,239,604.99	\$ 610,370,000.00	\$ 729,609,604.99

- (a) The estimate of future interest payments is based on rate in effect as of February 1, 2014, which is 0.04 .
\$500,000,000 of the Series 2009B Economic Recovery Bonds bear interest at fixed rates
ranging from 3.50 - 5.00 until reset date, and are assumed to bear interest at the rate of 4.00 from each reset date
to maturity.
- (b) Includes scheduled mandatory sinking fund payments.
- (c) Total represents the remaining estimated debt service requirements from March 1, 2014 through June 30, 2014.

SOURCE: State of California, Office of the Treasurer.

**SCHEDULE OF DEBT SERVICE REQUIREMENTS
FOR ENTERPRISE FUND SELF LIQUIDATING BONDS**

**Fixed Rate
As of February 1, 2014**

Fiscal Year Ending June 30	Current Debt			
	Interest	Principal	Total(a)	
2014	\$ 15,452,786.93	\$ 24,700,000.00	\$ 40,152,786.93	(b)
2015	31,000,520.58	77,565,000.00	108,565,520.58	
2016	27,986,964.13	75,620,000.00	103,606,964.13	
2017	25,286,280.00	61,895,000.00	87,181,280.00	
2018	22,599,282.15	60,655,000.00	83,254,282.15	
2019	20,419,911.16	35,900,000.00	56,319,911.16	
2020	18,939,693.75	28,115,000.00	47,054,693.75	
2021	17,613,488.75	19,570,000.00	37,183,488.75	
2022	16,700,878.78	13,630,000.00	30,330,878.78	
2023	16,133,431.25	9,695,000.00	25,828,431.25	
2024	15,822,096.25	4,365,000.00	20,187,096.25	
2025	15,620,462.30	4,660,000.00	20,280,462.30	
2026	15,516,388.75	-	15,516,388.75	
2027	15,140,813.65	16,695,000.00	31,835,813.65	
2028	14,565,072.80	8,835,000.00	23,400,072.80	
2029	13,781,762.80	25,075,000.00	38,856,762.80	
2030	12,252,673.69	40,325,000.00	52,577,673.69	
2031	10,301,552.28	42,490,000.00	52,791,552.28	
2032	8,707,392.50	25,755,000.00	34,462,392.50	
2033	7,508,072.50	26,690,000.00	34,198,072.50	
2034	6,359,375.00	22,705,000.00	29,064,375.00	
2035	5,269,037.50	23,310,000.00	28,579,037.50	
2036	4,403,300.00	13,945,000.00	18,348,300.00	
2037	3,548,333.75	23,025,000.00	26,573,333.75	
2038	2,662,880.00	15,300,000.00	17,962,880.00	
2039	1,950,055.00	16,025,000.00	17,975,055.00	
2040	1,195,310.00	16,790,000.00	17,985,310.00	
2041	404,570.00	17,590,000.00	17,994,570.00	
Total	\$ 367,142,386.25	\$ 750,925,000.00	\$ 1,118,067,386.25	

(a) Includes scheduled mandatory sinking fund payments.

(b) Total represents the remaining debt service requirements from March 1, 2014 through June 30, 2014.

SOURCE: State of California, Office of the Treasurer.

**STATE PUBLIC WORKS BOARD AND
OTHER LEASE-REVENUE FINANCING
OUTSTANDING ISSUES
As of February 1, 2014**

<u>Name of Issue</u>	<u>Outstanding</u>
<u>GENERAL FUND SUPPORTED ISSUES:</u>	
State Public Works Board	
California Community Colleges	\$ 333,975,000
California Department of Corrections and Rehabilitations	3,377,485,000
Trustees of the California State University	1,108,445,000
Various State Facilities (a)	5,032,990,000
Total State Public Works Board Issues	\$ 9,852,895,000
Total Other State Facilities Lease-Revenue Issues (b)	\$ 383,060,000
Total General Fund Supported Issues	\$ 10,235,955,000
<u>SPECIAL FUND SUPPORTED ISSUES:</u>	
East Bay State Building Authority	\$ 28,620,000
San Bernardino Joint Powers Financing Authority	27,930,000
Total Special Fund Supported Issues	\$ 56,550,000
TOTAL	\$ 10,292,505,000

(a) This includes projects that are supported by multiple funding sources in addition to the General Fund.

(b) Includes \$97,410,000 Sacramento City Financing Authority Lease-Revenue Refunding Bonds State of California - Cal/EPA Building, 2013 Series A, which are supported by lease rentals from the California Environmental Protection Agency; these rental payments are subject to annual appropriation by the State Legislature.

SOURCE: State of California, Office of the Treasurer.

**SCHEDULE OF DEBT SERVICE REQUIREMENTS
FOR LEASE-REVENUE DEBT**

Fixed Rate

As of February 1, 2014

Fiscal Year Ending June 30	Current Debt		
	Interest (a)	Principal	Total (b)
2014	\$ 255,981,851.44	\$ 166,365,000.00	\$ 422,346,851.44 (c)
2015	515,737,835.59	480,130,000.00	995,867,835.59
2016	492,792,073.47	509,525,000.00	1,002,317,073.47
2017	467,846,018.81	539,860,000.00	1,007,706,018.81
2018	440,768,034.20	578,745,000.00	1,019,513,034.20
2019	412,729,941.19	548,750,000.00	961,479,941.19
2020	385,485,123.07	530,610,000.00	916,095,123.07
2021	360,024,673.37	494,670,000.00	854,694,673.37
2022	335,214,440.42	478,595,000.00	813,809,440.42
2023	312,834,547.37	427,215,000.00	740,049,547.37
2024	291,422,200.29	410,385,000.00	701,807,200.29
2025	270,238,425.07	431,785,000.00	702,023,425.07
2026	248,025,641.91	437,360,000.00	685,385,641.91
2027	224,827,786.57	460,530,000.00	685,357,786.57
2028	200,585,264.73	469,055,000.00	669,640,264.73
2029	176,580,633.80	427,845,000.00	604,425,633.80
2030	153,365,491.93	417,945,000.00	571,310,491.93
2031	130,107,809.33	422,640,000.00	552,747,809.33
2032	105,791,828.34	426,130,000.00	531,921,828.34
2033	83,006,332.66	346,780,000.00	429,786,332.66
2034	62,073,049.00	354,915,000.00	416,988,049.00
2035	40,804,467.28	318,180,000.00	358,984,467.28
2036	25,483,625.00	181,200,000.00	206,683,625.00
2037	16,377,650.00	190,300,000.00	206,677,650.00
2038	6,813,925.00	128,275,000.00	135,088,925.00
2039	1,454,125.00	58,165,000.00	59,619,125.00
Total	\$ 6,016,372,794.84	\$ 10,235,955,000.00	\$ 16,252,327,794.84

(a) The amounts do not reflect any interest subsidy under the Build America Bonds program. Subsidy not pledged to the repayment of debt service.

(b) Includes scheduled mandatory sinking fund payments.

(c) Total represents the remaining debt service requirements from March 1, 2014 through June 30, 2014.

SOURCE: State of California, Office of the Treasurer.

**STATE AGENCY REVENUE BONDS
AND CONDUIT FINANCING
As of December 31, 2013**

<u>Issuing Agency</u>	<u>Outstanding</u> ^{(a)(b)(c)}
<u>State Revenue Bond Financing Programs:</u>	
California Alternative Energy and Advanced Transportation Financing Authority.....	\$ 13,333,333
California Department of Transportation - GARVEE.....	201,805,000
California Earthquake Authority.....	94,500,000
California Health Facilities Financing Authority.....	69,955,000
California Housing Finance Agency.....	4,029,271,714
California Infrastructure and Economic Development Bank.....	529,313,000
California State University.....	3,507,043,000
Department of Water Resources - Central Valley Project.....	2,294,200,000
Department of Water Resources - Power Supply Program.....	6,553,805,000
The Regents of the University of California.....	14,574,465,000
Veterans Revenue Debenture.....	376,790,000
TOTAL.....	\$ 32,244,481,047
<u>Conduit Financing:</u>	
California Alternative Energy and Advanced Transportation Financing Authority.....	\$ 57,681,809
California Educational Facilities Authority.....	4,455,892,819
California Health Facilities Financing Authority.....	12,939,347,152
California Housing Finance Agency.....	337,793,676
California Infrastructure and Economic Development Bank	4,078,998,619
California Pollution Control Financing Authority.....	3,900,124,873
California School Financing Authority.....	205,420,000
California Student Loan Authority.....	5,100,000
TOTAL.....	\$ 25,980,358,948

- (a) Totals for California Department of Transportation, California State University, Department of Water Resources and Veterans Revenue Debenture were provided by the State of California, Office of the Treasurer. All other totals were provided by the listed issuing agency.
- (b) Does not include the Tobacco Settlement Revenue Bonds issued by Golden State Tobacco Securitization Corporation.
- (c) Certain state agencies and authorities issue revenue obligations for which the General Fund has no liability. See "STATE INDEBTEDNESS AND OTHER OBLIGATIONS – Capital Facilities Financing -Non-Recourse Debt." The tables above are intended to provide general information concerning the scope of the various State Revenue Bond Financing and Conduit Financing Programs referenced therein, and are not intended to be an exhaustive listing of all of the outstanding obligations of the respective programs.

STATEMENT of GENERAL FUND CASH RECEIPTS and DISBURSEMENTS

June 2013



JOHN CHIANG
California State Controller &



JOHN CHIANG
California State Controller

July 10, 2013

Users of the Statement of General Fund Cash Receipts and Disbursements: &

Enclosed is the Statement of General Fund Cash Receipts and Disbursements for the period July 1, 2012, through June 30, 2013. This statement reflects the State of California's General Fund cash position and compares actual receipts and disbursements for the 2012-13 Fiscal Year to cash flow estimates prepared by the Department of Finance for the 2012 Budget Act. The statement is prepared in compliance with Provision 7 of Budget Act item 0840-001-0001, using records compiled by the State Controller. Prior year actual amounts are also displayed for comparative purposes.

Attachment A compares actual receipts and disbursements for the 2012-13 fiscal year to cash flow estimates published in the 2013-14 May Revision Budget. These cash flow estimates are predicated on projections and assumptions made by the Department of Finance in preparation of the May Revision Budget.

Attachment B compares actual receipts and disbursements for the 2012-13 fiscal year to cash flow estimates prepared by the Department of Finance based upon the 2012 Budget Act.

These statements are also available on the Internet at the State Controller's website at www.sco.ca.gov under the category Monthly Financial Reports.

Any questions concerning this report may be directed to George Lolas, Division Chief of Accounting and Reporting, at (916) 322-7407.

Sincerely,
Original signed by:

JOHN CHIANG
California State Controller

STATEMENT OF GENERAL FUND CASH RECEIPTS AND DISBURSEMENTS
A Comparison of Actual to 2013-14 May Revision Estimates
(Amounts in thousands)

	July 1 through June 30				
	2013				2012
	Actual	Estimate (a)	Actual Over or (Under) Estimate		Actual
			Amount		
GENERAL FUND BEGINNING CASH BALANCE	\$ -	\$ -	\$ -	-	\$ -
Add Receipts:					
Revenues	100,078,372	98,079,845	1,998,527	2.0	83,473,884
Nonrevenues	3,346,302	3,207,868	138,434	4.3	4,295,903
Total Receipts	103,424,674	101,287,713	2,136,961	2.1	87,769,787
Less Disbursements:					
State Operations	26,130,710	23,781,752	2,348,958	9.9	24,431,344
Local Assistance	68,095,108	71,066,384	(2,971,276)	(4.2)	64,579,659
Capital Outlay	117,388	164,030	(46,642)	(28.4)	190,873
Nongovernmental	1,923,042	947,692	975,350	-	(3,262)
Total Disbursements	96,266,248	95,959,858	306,390	0.3	89,198,614
Receipts Over / (Under) Disbursements	7,158,426	5,327,855	1,830,571	34.4	(1,428,827)
Net Increase / (Decrease) in Temporary Loans	(7,158,426)	(5,327,855)	(1,830,571)	-	1,428,827
GENERAL FUND ENDING CASH BALANCE	-	-	-		-
Special Fund for Economic Uncertainties	-	-	-	-	-
TOTAL CASH	\$ -	\$ -	\$ -		\$ -
BORROWABLE RESOURCES					
Available Borrowable Resources	\$ 21,215,251	\$ 19,077,200	\$ 2,138,051	11.2	\$ 20,824,299
Outstanding Loans (b)	2,434,865	4,265,434	(1,830,569)	(42.9)	9,593,291
Unused Borrowable Resources	\$ 18,780,386	\$ 14,811,766	\$ 3,968,620	26.8	\$ 11,231,008

General Note:

This report is based upon funded cash. Funded cash is cash reported to and recorded in the records of the State Controller's Office. Amounts reported as funded cash may differ from amounts in other reports to the extent there are timing differences in the recording of in-transit items.

Footnotes:

- A Statement of Estimated Cash Flow for the 2012-13 fiscal year was prepared by the Department of Finance for the 2013-14 May Revision. Any projections or estimates are set forth as such and not as representation of facts.
- Outstanding loan balance of \$2.4 billion is comprised of \$2.4 billion of internal borrowing. Current balance is comprised of \$9.6 billion carried forward from June 30, 2012, plus current year Net Increase/(Decrease) in Temporary Loans of (\$7.2) billion. \$2.5 billion of RANs were repaid in May 2013 and \$7.5 billion of RANS were repaid in June 2013 as scheduled.
- Negative amounts are the result of repayments received that are greater than disbursements made.
- Debt Service amounts are net of offsets such as federal subsidies and reimbursements from other sources. To the extent that these offsets do not occur when anticipated, there can be variances between actuals and estimates on a month-to-month basis.

Continued on page A2.

SCHEDULE OF CASH RECEIPTS

(Amounts in thousands)

	Month of June		July 1 through June 30					
			2013			2012		
	2013	2012	Actual	Estimate (a)	Actual Over or (Under) Estimate		Actual	
					Amount			
REVENUES								
Alcoholic Beverage Excise Tax	\$ 29,418	\$ 22,860	\$ 360,803	\$ 330,849	\$ 29,954	9.1	\$ 338,178	
Corporation Tax	2,112,500	1,664,304	7,620,406	7,224,338	396,068	5.5	8,051,423	
Cigarette Tax	13,163	8,290	91,172	90,358	814	0.9	100,906	
Estate, Inheritance, and Gift Tax	371	478	4,303	3,693	610	16.5	3,991	
Insurance Companies Tax	326,110	348,161	2,244,313	2,157,876	86,437	4.0	2,187,463	
Personal Income Tax	8,029,598	6,914,343	67,314,600	66,073,435	1,241,165	1.9	50,699,002	
Retail Sales and Use Taxes	2,050,138	1,781,338	20,073,343	19,985,405	87,938	0.4	19,438,408	
Vehicle License Fees	261	1,104	7,493	6,763	730	10.8	83,406	
Pooled Money Investment Interest	4,178	4,691	23,426	23,296	130	0.6	25,605	
Not Otherwise Classified	558,666	635,030	2,338,513	2,183,832	154,681	-	2,545,502	
Total Revenues	13,124,403	11,380,599	100,078,372	98,079,845	1,998,527	2.0	83,473,884	
NONREVENUES								
Transfers from Special Fund for Economic Uncertainties	-	-	-	-	-	-	715,854	
Transfers from Other Funds	340,873	338,557	2,051,308	1,954,004	97,304	5.0	2,348,551	
Miscellaneous	38,652	75,018	1,294,994	1,253,864	41,130	3.3	1,231,498	
Total Nonrevenues	379,525	413,575	3,346,302	3,207,868	138,434	4.3	4,295,903	
Total Receipts	\$ 13,503,928	\$ 11,794,174	\$ 103,424,674	\$ 101,287,713	\$ 2,136,961	2.1	\$ 87,769,787	

See notes on page A1 and A2.

- (e) A \$1.0 billion advance was made from the General Fund to the Medi-Cal Provider Interim Payment Fund and repayment is anticipated in July 2013. Consequently, the disbursements for Local Assistance Medical Assistance program will increase in July.
- (f) Redemption of \$1.9 billion of Prop 1A obligations are accounted for under State Operations, General Government, while this amount was included in Department of Finance projections under Local Assistance, Other Local Assistance.

SCHEDULE OF CASH DISBURSEMENTS

(Amounts in thousands)

	Month of June		July 1 through June 30					2012
			2013					
	2013	2012	Actual	Estimate (a)	Actual Over or (Under) Estimate		Actual	
					Amount			
STATE OPERATIONS (c)								
Legislative/Judicial/Executive	\$ 73,106	\$ 101,831	\$ 1,000,838	\$ 1,105,999	\$ (105,161)	(9.5)	\$ 1,253,131	
State and Consumer Services	48,269	50,175	663,371	679,646	(16,275)	(2.4)	590,961	
Business, Transportation and Housing	269	989	3,978	3,412	566	-	26,876	
Resources	59,696	26,455	1,143,350	1,100,729	42,621	3.9	929,868	
Environmental Protection Agency	3,169	3,910	34,023	41,510	(7,487)	(18.0)	35,694	
Health and Human Services:								
Health Services	16,949	20,666	217,429	236,328	(18,899)	(8.0)	222,734	
Mental Health	65,279	93,712	1,161,511	1,227,814	(66,303)	(5.4)	1,232,235	
Other Health and Human Services	(14,830)	(12,771)	469,474	513,110	(43,636)	(8.5)	967,807	
Education:								
University of California	502,167	651,602	2,386,114	2,396,751	(10,637)	(0.4)	2,277,772	
State Universities and Colleges	62,144	(56)	2,244,988	2,063,549	181,439	8.8	1,999,976	
Other Education	10,901	11,547	169,881	175,289	(5,408)	(3.1)	164,030	
Dept. of Corrections and Rehabilitation	646,220	560,848	7,788,842	7,774,638	14,204	0.2	7,991,944	
General Government	2,105,094	165,271	4,270,890	2,331,922	1,938,968	(f) 83.1	1,914,058	
Public Employees Retirement								
System	(145,308)	(142,535)	(6,616)	(12,342)	5,726	-	(6,331)	
Debt Service (d)	473,119	432,064	4,482,775	4,197,570	285,205	6.8	4,744,822	
Interest on Loans	161,738	83,548	99,862	(54,173)	154,035	-	85,767	
Total State Operations	4,067,982	2,047,256	26,130,710	23,781,752	2,348,958	9.9	24,431,344	
LOCAL ASSISTANCE (c)								
Public Schools - K-12	6,880,525	570,189	36,476,720	36,531,912	(55,192)	(0.2)	29,269,540	
Community Colleges	842,868	100,095	3,584,580	3,590,300	(5,720)	(0.2)	3,284,018	
Debt Service-School Building Bonds	-	-	-	(379)	379	-	-	
Contributions to State Teachers'								
Retirement System	-	-	1,359,675	1,359,675	-	-	1,316,108	
Other Education	(27,177)	34,209	1,813,620	1,984,526	(170,906)	(8.6)	3,482,653	
School Facilities Aid	-	-	-	379	(379)	(100.0)	-	
Dept. of Corrections and Rehabilitation	3,009	1,837	223,654	217,976	5,678	2.6	234,339	
Dept. of Alcohol and Drug Program	1,583	(18,487)	42,770	44,223	(1,453)	(3.3)	53,548	
Dept. of Health Services:								
Medical Assistance Program	99,102	579,231	14,391,478	14,948,799	(557,321)	(e) (3.7)	15,096,282	
Other Health Services	10,178	(24,746)	108,352	165,076	(56,724)	(34.4)	24,062	
Dept. of Developmental Services	(21,128)	42,600	2,037,886	2,056,259	(18,373)	(0.9)	2,097,430	
Dept. of Mental Health	-	148,745	10,664	10,664	-	-	357,495	
Dept. of Social Services:								
SSI/SSP/IHSS	300,849	391,185	4,453,798	4,440,846	12,952	0.3	4,497,175	
CalWORKs	55,369	95,818	1,348,177	1,292,888	55,289	4.3	1,744,646	
Other Social Services	37,388	28,148	682,154	685,819	(3,665)	(0.5)	827,068	
Tax Relief	-	-	427,285	422,719	4,566	1.1	433,008	
Other Local Assistance	52,554	82,048	1,134,295	3,314,702	(2,180,407)	(f) (65.8)	1,862,287	
Total Local Assistance	8,235,120	2,030,872	68,095,108	71,066,384	(2,971,276)	(4.2)	64,579,659	

See notes on page A1 and A2.

(Continued)

SCHEDULE OF CASH DISBURSEMENTS (Continued)

(Amounts in thousands)

	Month of June		July 1 through June 30				2012
	2013	2012	Actual	Estimate (a)	Actual Over or (Under) Estimate		Actual
					Amount		
CAPITAL OUTLAY	8,870	5,800	117,388	164,030	(46,642)	(28.4)	190,873
NONGOVERNMENTAL (c)							
Transfer to Special Fund for Economic Uncertainties	-	-	473,243	473,243	-	-	-
Transfer to Budget Stabilization Account	-	-	-	-	-	-	-
Transfer to Other Funds	43,740	81,149	404,748	403,708	1,040	0.3	339,670
Transfer to Revolving Fund	(10,989)	(38,286)	(9,808)	5,676	(15,484)	(272.8)	(44,495)
Advance:							
MediCal Provider Interim Payment	-	-	1,000,000	-	1,000,000	(e)	-
State-County Property Tax Administration Program	(4,380)	(31,995)	18,682	45,637	(26,955)	(59.1)	6,459
Social Welfare Federal Fund	28,000	29,000	(63,763)	(91,763)	28,000	-	(39,483)
Local Governmental Entities	-	-	60,000	60,000	-	-	-
Tax Relief and Refund Account	-	-	-	-	-	-	-
Counties for Social Welfare	315,672	275,732	39,940	51,191	(11,251)	(22.0)	(265,413)
Total Nongovernmental	372,043	315,600	1,923,042	947,692	975,350	-	(3,262)
Total Disbursements	\$ 12,684,015	\$ 4,399,528	\$ 96,266,248	\$ 95,959,858	\$ 306,390	0.3	\$ 89,198,614
TEMPORARY LOANS							
Special Fund for Economic Uncertainties	\$ 948,200	\$ -	\$ 473,243	\$ 473,243	\$ -	-	\$ (715,854)
Budget Stabilization Account	-	-	-	-	-	-	-
Outstanding Registered Warrants Account	-	-	-	-	-	-	-
Other Internal Sources	1,486,665	(1,494,646)	(7,631,669)	(5,801,098)	(1,830,571)	-	2,144,681
Revenue Anticipation Notes	(7,500,000)	(5,900,000)	-	-	-	-	-
Net Increase / (Decrease) Loans	(5,065,135)	\$ (7,394,646)	\$ (7,158,426)	\$ (5,327,855)	\$ (1,830,571)	-	\$ 1,428,827

See notes on page A1 and A2.

(Concluded)

COMPARATIVE STATEMENT OF REVENUES RECEIVED
All Governmental Cost Funds
(Amounts in thousands)

	July 1 through June 30			
	General Fund		Special Funds	
	2013	2012	2013	2012
MAJOR TAXES, LICENSES, AND INVESTMENT INCOME:				
Alcoholic Beverage Excise Taxes	\$ 360,803	\$ 338,178	\$ -	\$ -
Corporation Tax	7,620,406	8,051,423	-	-
Cigarette Tax	91,172	100,906	776,194	855,784
Estate, Inheritance, and Gift Tax	4,303	3,991	-	36
Insurance Companies Tax	2,244,313	2,187,463	34,389	250,547
Motor Vehicle Fuel Tax:				
Gasoline Tax	-	-	5,196,201	5,203,059
Diesel & Liquid Petroleum Gas	-	-	333,028	404,312
Jet Fuel Tax	-	-	2,406	2,536
Vehicle License Fees	7,493	83,406	1,971,800	1,967,890
Motor Vehicle Registration and Other Fees	-	-	3,920,199	3,894,213
Personal Income Tax	67,314,600	50,699,002	1,200,346	-
Retail Sales and Use Taxes	20,073,343	19,438,408	13,355,024	12,047,491
Pooled Money Investment Interest	23,426	25,605	181	314
Total Major Taxes, Licenses, and Investment Income	97,739,859	80,928,382	26,789,768	24,626,182
NOT OTHERWISE CLASSIFIED:				
Alcoholic Beverage License Fee	2,479	3,538	52,136	53,967
Electrical Energy Tax	-	-	712,069	788,020
Private Rail Car Tax	7,893	8,041	-	-
Penalties on Traffic Violations	-	-	74,526	80,652
Health Care Receipts	18,442	39,237	-	-
Revenues from State Lands	422,475	480,831	-	-
Abandoned Property	474,738	520,294	-	-
Trial Court Revenues	51,251	55,070	1,701,124	1,715,152
Horse Racing Fees	1,117	1,176	13,461	15,746
Cap and Trade	-	-	257,264	-
Miscellaneous	1,360,118	1,437,315	11,754,098	6,755,288
Not Otherwise Classified	2,338,513	2,545,502	14,564,678	9,408,825
Total Revenues, All Governmental Cost Funds	\$ 100,078,372	\$ 83,473,884	\$ 41,354,446	\$ 34,035,007

See notes on page A1 and A2.

STATEMENT OF GENERAL FUND CASH RECEIPTS AND DISBURSEMENTS
A Comparison of Actual to 2012 Budget Act
(Amounts in thousands)

	July 1 through June 30				
	2013				2012
	Actual	Estimate (a)	Actual Over or (Under) Estimate		Actual
			Amount		
GENERAL FUND BEGINNING CASH BALANCE	\$ -	\$ -	\$ -	-	\$ -
Add Receipts:					
Revenues	100,078,372	96,678,993	3,399,379	3.5	83,473,884
Nonrevenues	3,346,302	2,532,746	813,556	32.1	4,295,903
Total Receipts	103,424,674	99,211,739	4,212,935	4.2	87,769,787
Less Disbursements:					
State Operations	26,130,710	24,671,958	1,458,752	5.9	24,431,344
Local Assistance	68,095,108	69,406,396	(1,311,288)	(1.9)	64,579,659
Capital Outlay	117,388	178,150	(60,762)	(34.1)	190,873
Nongovernmental	1,923,042	957,549	965,493	-	(3,262)
Total Disbursements	96,266,248	95,214,053	1,052,195	1.1	89,198,614
Receipts Over / (Under) Disbursements	7,158,426	3,997,686	3,160,740	79.1	(1,428,827)
Net Increase / (Decrease) in Temporary Loans	(7,158,426)	(3,997,686)	(3,160,740)	-	1,428,827
GENERAL FUND ENDING CASH BALANCE	-	-	-		-
Special Fund for Economic Uncertainties			-	-	-
TOTAL CASH	\$ -	\$ -	\$ -		\$ -
BORROWABLE RESOURCES					
Available Borrowable Resources	\$ 21,215,251	\$ 19,028,200	\$ 2,187,051	11.5	\$ 20,824,299
Outstanding Loans (b)	2,434,865	5,595,603	(3,160,738)	(56.5)	9,593,291
Unused Borrowable Resources	\$ 18,780,386	\$ 13,432,597	\$ 5,347,789	39.8	\$ 11,231,008

General Note:

This report is based upon funded cash. Funded cash is cash reported to and recorded in the records of the State Controller's Office. Amounts reported as funded cash may differ from amounts in other reports to the extent there are timing differences in the recording of in-transit items.

Footnotes:

- (a) A Statement of Estimated Cash Flow for the 2012-13 fiscal year was prepared by the Department of Finance for the 2012 Budget Act. Any projections or estimates are set forth as such and not as representation of facts.
- (b) Outstanding loan balance of \$2.4 billion is comprised of \$2.4 billion of internal borrowing. Current balance is comprised of \$9.6 billion carried forward from June 30, 2012, plus current year Net Increase/(Decrease) in Temporary Loans of (\$7.2) billion. \$2.5 billion of RANS were repaid in May 2013 and \$7.5 billion of RANS were repaid in June 2013 as scheduled.
- (c) Negative amounts are the result of repayments received that are greater than disbursements made.
- (d) Debt Service amounts are net of offsets such as federal subsidies and reimbursements from other sources. To the extent that these offsets do not occur when anticipated, there can be variances between actuals and estimates on a month-to-month basis.

Continued on page B2.

SCHEDULE OF CASH RECEIPTS

(Amounts in thousands)

	Month of June		July 1 through June 30				
			2013			2012	
	2013	2012	Actual	Estimate (a)	Actual Over or (Under) Estimate		Actual
					Amount		
REVENUES							
Alcoholic Beverage Excise Tax	\$ 29,418	\$ 22,860	\$ 360,803	\$ 339,000	\$ 21,803	6.4	\$ 338,178
Corporation Tax	2,112,500	1,664,304	7,620,406	8,414,000	(793,594)	(9.4)	8,051,423
Cigarette Tax	13,163	8,290	91,172	93,000	(1,828)	(2.0)	100,906
Estate, Inheritance, and Gift Tax	371	478	4,303	-	4,303	-	3,991
Insurance Companies Tax	326,110	348,161	2,244,313	2,088,000	156,313	7.5	2,187,463
Personal Income Tax	8,029,598	6,914,343	67,314,600	62,801,000	4,513,600	7.2	50,699,002
Retail Sales and Use Taxes	2,050,138	1,781,338	20,073,343	20,374,600	(301,257)	(1.5)	19,438,408
Vehicle License Fees	261	1,104	7,493	3,000	4,493	149.8	83,406
Pooled Money Investment Interest	4,178	4,691	23,426	30,000	(6,574)	(21.9)	25,605
Not Otherwise Classified	558,666	635,030	2,338,513	2,536,393	(197,880)	-	2,545,502
Total Revenues	13,124,403	11,380,599	100,078,372	96,678,993	3,399,379	3.5	83,473,884
NONREVENUES							
Transfers from Special Fund for Economic Uncertainties	-	-	-	-	-	-	715,854
Transfers from Other Funds	340,873	338,557	2,051,308	1,810,575	240,733	13.3	2,348,551
Miscellaneous	38,652	75,018	1,294,994	722,171	572,823	79.3	1,231,498
Total Nonrevenues	379,525	413,575	3,346,302	2,532,746	813,556	32.1	4,295,903
Total Receipts	\$ 13,503,928	\$ 11,794,174	\$ 103,424,674	\$ 99,211,739	\$ 4,212,935	4.2	\$ 87,769,787

See notes on page B1 and B2.

- (e) A \$1.0 billion advance was made from the General Fund to the Medi-Cal Provider Interim Payment Fund and repayment is anticipated in July 2013. Consequently, the disbursements for Local Assistance Medical Assistance program will increase in July.
- (f) Redemption of \$1.9 billion of Prop 1A obligations are accounted for under State Operations, General Government, while this amount was included in Department of Finance projections under Local Assistance, Other Local Assistance.

SCHEDULE OF CASH DISBURSEMENTS

(Amounts in thousands)

	Month of June		July 1 through June 30					2012
			2013					
	2013	2012	Actual	Estimate (a)	Actual Over or (Under) Estimate		Actual	
					Amount			
STATE OPERATIONS (c)								
Legislative/Judicial/Executive	\$ 73,106	\$ 101,831	\$ 1,000,838	\$ 1,425,157	\$ (424,319)	(29.8)	\$ 1,253,131	
State and Consumer Services	48,269	50,175	663,371	689,135	(25,764)	(3.7)	590,961	
Business, Transportation and Housing	269	989	3,978	1,431	2,547	-	26,876	
Resources	59,696	26,455	1,143,350	1,010,915	132,435	13.1	929,868	
Environmental Protection Agency	3,169	3,910	34,023	41,252	(7,229)	(17.5)	35,694	
Health and Human Services:								
Health Services	16,949	20,666	217,429	231,013	(13,584)	(5.9)	222,734	
Mental Health	65,279	93,712	1,161,511	1,288,500	(126,989)	(9.9)	1,232,235	
Other Health and Human Services	(14,830)	(12,771)	469,474	526,879	(57,405)	(10.9)	967,807	
Education:								
University of California	502,167	651,602	2,386,114	2,384,855	1,259	0.1	2,277,772	
State Universities and Colleges	62,144	(56)	2,244,988	2,250,902	(5,914)	(0.3)	1,999,976	
Other Education	10,901	11,547	169,881	129,475	40,406	31.2	164,030	
Dept. of Corrections and Rehabilitation	646,220	560,848	7,788,842	8,573,380	(784,538)	(9.2)	7,991,944	
General Government	2,105,094	165,271	4,270,890	1,583,787	2,687,103	(f) 169.7	1,914,058	
Public Employees Retirement								
System	(145,308)	(142,535)	(6,616)	(17,264)	10,648	-	(6,331)	
Debt Service (d)	473,119	432,064	4,482,775	4,348,541	134,234	3.1	4,744,822	
Interest on Loans	161,738	83,548	99,862	204,000	(104,138)	-	85,767	
Total State Operations	4,067,982	2,047,256	26,130,710	24,671,958	1,458,752	5.9	24,431,344	
LOCAL ASSISTANCE (c)								
Public Schools - K-12	6,880,525	570,189	36,476,720	35,619,519	857,201	2.4	29,269,540	
Community Colleges	842,868	100,095	3,584,580	3,635,123	(50,543)	(1.4)	3,284,018	
Debt Service-School Building Bonds	-	-	-	(389)	389	-	-	
Contributions to State Teachers'								
Retirement System	-	-	1,359,675	1,359,675	-	-	1,316,108	
Other Education	(27,177)	34,209	1,813,620	1,568,514	245,106	15.6	3,482,653	
School Facilities Aid	-	-	-	389	(389)	(100.0)	-	
Dept. of Corrections and Rehabilitation	3,009	1,837	223,654	170,572	53,082	31.1	234,339	
Dept. of Alcohol and Drug Program	1,583	(18,487)	42,770	9,500	33,270	350.2	53,548	
Dept. of Health Services:								
Medical Assistance Program	99,102	579,231	14,391,478	14,218,407	173,071	(e) 1.2	15,096,282	
Other Health Services	10,178	(24,746)	108,352	388,152	(279,800)	(72.1)	24,062	
Dept. of Developmental Services	(21,128)	42,600	2,037,886	1,727,392	310,494	18.0	2,097,430	
Dept. of Mental Health	-	148,745	10,664	13,130	(2,466)	(18.8)	357,495	
Dept. of Social Services:								
SSI/SSP/IHSS	300,849	391,185	4,453,798	4,474,341	(20,543)	(0.5)	4,497,175	
CalWORKs	55,369	95,818	1,348,177	1,711,682	(363,505)	(21.2)	1,744,646	
Other Social Services	37,388	28,148	682,154	673,540	8,614	1.3	827,068	
Tax Relief	-	-	427,285	433,152	(5,867)	(1.4)	433,008	
Other Local Assistance	52,554	82,048	1,134,295	3,403,697	(2,269,402)	(f) (66.7)	1,862,287	
Total Local Assistance	8,235,120	2,030,872	68,095,108	69,406,396	(1,311,288)	(1.9)	64,579,659	

See notes on page B1 and B2.

(Continued)

SCHEDULE OF CASH DISBURSEMENTS (Continued)

(Amounts in thousands)

	Month of June		July 1 through June 30				2012
	2013	2012	Actual	Estimate (a)	Actual Over or (Under) Estimate		Actual
					Amount		
CAPITAL OUTLAY	8,870	5,800	117,388	178,150	(60,762)	(34.1)	190,873
NONGOVERNMENTAL (c)							
Transfer to Special Fund for Economic Uncertainties	-	-	473,243	473,243	-	-	-
Transfer to Budget Stabilization Account	-	-	-	-	-	-	-
Transfer to Other Funds	43,740	81,149	404,748	494,262	(89,514)	(18.1)	339,670
Transfer to Revolving Fund	(10,989)	(38,286)	(9,808)	-	(9,808)	-	(44,495)
Advance:							
MediCal Provider Interim Payment	-	-	1,000,000	-	1,000,000	(e)	-
State-County Property Tax Administration Program	(4,380)	(31,995)	18,682	-	18,682	-	6,459
Social Welfare Federal Fund	28,000	29,000	(63,763)	-	(63,763)	-	(39,483)
Local Governmental Entities	-	-	60,000	-	60,000	-	-
Tax Relief and Refund Account	-	-	-	-	-	-	-
Counties for Social Welfare	315,672	275,732	39,940	(9,956)	49,896	-	(265,413)
Total Nongovernmental	372,043	315,600	1,923,042	957,549	965,493	-	(3,262)
Total Disbursements	\$ 12,684,015	\$ 4,399,528	\$ 96,266,248	\$ 95,214,053	\$ 1,052,195	1.1	\$ 89,198,614
TEMPORARY LOANS							
Special Fund for Economic Uncertainties	\$ 948,200	\$ -	\$ 473,243	\$ 473,243	\$ -	-	\$ (715,854)
Budget Stabilization Account	-	-	-	-	-	-	-
Outstanding Registered Warrants Account	-	-	-	-	-	-	-
Other Internal Sources	1,486,665	(1,494,646)	(7,631,669)	(4,470,929)	(3,160,740)	-	2,144,681
Revenue Anticipation Notes	(7,500,000)	(5,900,000)	-	-	-	-	-
Net Increase / (Decrease) Loans	(5,065,135)	\$ (7,394,646)	\$ (7,158,426)	\$ (3,997,686)	\$ (3,160,740)	-	\$ 1,428,827

See notes on page B1 and B2.

(Concluded)

STATEMENT of GENERAL FUND CASH RECEIPTS and DISBURSEMENTS

February 2014



JOHN CHIANG
California State Controller &



JOHN CHIANG
California State Controller

March 10, 2014

Users of the Statement of General Fund Cash Receipts and Disbursements: &

Enclosed is the Statement of General Fund Cash Receipts and Disbursements for the period July 1, 2013, through February 28, 2014. This statement reflects the State of California's General Fund cash position and compares actual receipts and disbursements for the 2013-14 fiscal year to cash flow estimates prepared by the Department of Finance (DOF) for the 2013-14 Budget Act. The statement is prepared in compliance with Provision 7 of Budget Act item 0840-001-0001, using records compiled by the State Controller. Prior year actual amounts are also displayed for comparative purposes.

Attachment A compares actual receipts and disbursements for the 2013-14 fiscal year to cash flow estimates published in the 2014-15 Governor's Budget. These cash flow estimates are predicated on projections and assumptions made by the DOF in preparation of the 2014-15 Governor's Budget.

Attachment B compares actual receipts and disbursements for the 2013-14 fiscal year to cash flow estimates prepared by the Department of Finance based upon the 2013-14 Budget Act.

These statements are also available on the Internet at the State Controller's website at www.sco.ca.gov under the category Monthly Financial Reports.

Any questions concerning this report may be directed to Casandra Moore-Hudnall, Division Chief of Accounting and Reporting, by telephone at (916) 445-5834.

Sincerely,
Original signed by:

JOHN CHIANG
California State Controller

STATEMENT OF GENERAL FUND CASH RECEIPTS AND DISBURSEMENTS
A Comparison of Actual to 2014-15 Governor's Budget Estimates
(Amounts in thousands)

	July 1 through February 28				
	2014				2013
	Actual	Estimate (a)	Actual Over or (Under) Estimate		Actual
			Amount		
GENERAL FUND BEGINNING CASH BALANCE	\$ -	\$ -	\$ -	-	\$ -
Add Receipts:					
Revenues	59,798,484	58,402,091	1,396,393	2.4	58,761,236
Nonrevenues	1,710,529	1,566,306	144,223	9.2	2,146,516
Total Receipts	61,509,013	59,968,397	1,540,616	2.6	60,907,752
Less Disbursements:					
State Operations	17,335,469	17,685,386	(349,917)	(2.0)	15,333,793
Local Assistance	56,448,949	56,774,742	(325,793)	(0.6)	51,493,059
Capital Outlay	133,645	147,768	(14,123)	(9.6)	103,172
Nongovernmental	(704,117)	(753,284)	49,167	-	606,139
Total Disbursements	73,213,946	73,854,612	(640,666)	(0.9)	67,536,163
Receipts Over / (Under) Disbursements	(11,704,933)	(13,886,215)	2,181,282	-	(6,628,411)
Net Increase / (Decrease) in Temporary Loans	11,704,933	13,886,215	(2,181,282)	(15.7)	6,628,411
GENERAL FUND ENDING CASH BALANCE	-	-	-		-
Special Fund for Economic Uncertainties	-	-	-	-	-
TOTAL CASH	\$ -	\$ -	\$ -		\$ -
Borrowable Resources					
Available Borrowable Resources	\$ 28,392,111	\$ 26,069,100	\$ 2,323,011	(e) 8.9	\$ 33,650,891
Outstanding Loans (b)	14,139,798	16,321,079	(2,181,281)	(13.4)	16,221,702
Unused Borrowable Resources	\$ 14,252,313	\$ 9,748,021	\$ 4,504,292	46.2	\$ 17,429,189

General Note:

This report is based upon funded cash. Funded cash is cash reported to and recorded in the records of the State Controller's Office. Amounts reported as funded cash may differ from amounts in other reports to the extent there are timing differences in the recording of in-transit items.

Footnotes:

- (a) %A Statement of Estimated Cash Flow for the 2013-14 fiscal year was prepared by the Department of Finance for the 2014-15 Governor's Budget. Any projections or estimates are set forth as such and not as representation of facts.
- (b) %Outstanding loan balance of \$14.1 billion is comprised of \$8.6 billion of internal borrowing and \$5.5 billion of external borrowing. Current balance is comprised of \$2.4 billion carried forward from June 30, 2013, plus current year Net Increase/(Decrease) in Temporary Loans of \$11.7 billion.
- (c) %Negative amounts are the result of repayments received that are greater than disbursements made.
- (d) %Debt Service amounts are net of offsets such as federal subsidies and reimbursements from other sources. To the extent that these offsets do not occur when anticipated, there can be variances between actuals and estimates on a month-to-month basis.
- (e) On August 22, 2013, \$5.5 billion of Revenue Anticipation Notes (RANs) proceeds were received.

SCHEDULE OF CASH RECEIPTS

(Amounts in thousands)

	Month of February		July 1 through February 28				
			2014			2013	
	2014	2013	Actual	Estimate (a)	Actual Over or (Under) Estimate		Actual
					Amount		
REVENUES							
Alcoholic Beverage Excise Tax	\$ 27,295	\$ 41,405	\$ 236,449	\$ 211,939	\$ 24,510	11.6	\$ 221,592
Corporation Tax	124,382	144,347	2,838,801	2,535,245	303,556	12.0	2,292,843
Cigarette Tax	6,611	6,329	58,608	59,994	(1,386)	(2.3)	61,791
Estate, Inheritance, and Gift Tax	421	898	6,106	4,605	1,501	32.6	3,353
Insurance Companies Tax	16,877	18,055	1,147,101	1,137,895	9,206	0.8	1,105,131
Personal Income Tax	2,300,732	1,926,806	39,873,023	38,879,331	993,692	2.6	40,795,345
Retail Sales and Use Taxes	3,012,661	2,993,544	14,682,171	14,739,625	(57,454)	(0.4)	12,963,107
Vehicle License Fees	108	458	1,666	1,302	364	28.0	5,679
Pooled Money Investment Interest	537	732	14,940	13,877	1,063	7.7	14,615
Not Otherwise Classified	120,302	152,637	939,619	818,278	121,341	-	1,297,780
Total Revenues	5,609,926	5,285,211	59,798,484	58,402,091	1,396,393	2.4	58,761,236
NONREVENUES							
Transfers from Special Fund for Economic Uncertainties	-	-	-	-	-	-	-
Transfers from Other Funds	44,501	91,717	902,132	891,439	10,693	1.2	1,391,453
Miscellaneous	218,795	212,478	808,397	674,867	133,530	19.8	755,063
Total Nonrevenues	263,296	304,195	1,710,529	1,566,306	144,223	9.2	2,146,516
Total Receipts	\$ 5,873,222	\$ 5,589,406	\$ 61,509,013	\$ 59,968,397	\$ 1,540,616	2.6	\$ 60,907,752

See notes on page A1.

SCHEDULE OF CASH DISBURSEMENTS

(Amounts in thousands)

	Month of February		July 1 through February 28					2013
	2014	2013	Actual	Estimate (a)	Actual Over or (Under) Estimate		Actual	
					Amount			
STATE OPERATIONS (c)								
Legislative/Judicial/Executive	\$ 113,948	\$ 116,938	\$ 1,167,948	\$ 1,089,806	\$ 78,142	7.2	\$ 667,021	
Business, Consumer Services and Housing	943	91,196	11,572	10,943	629	5.7	471,532	
Transportation	-	56	464	345	119	-	2,710	
Resources	43,043	44,130	774,893	737,261	37,632	5.1	846,299	
Environmental Protection Agency	2,211	5,388	27,610	27,705	(95)	(0.3)	23,275	
Health and Human Services:								
Health Care Services and Public Health	19,285	65,164	213,369	212,760	609	0.3	204,875	
Department of State Hospitals	123,241	99,749	918,076	925,625	(7,549)	(0.8)	782,208	
Other Health and Human Services	22,993	57,379	427,141	424,617	2,524	0.6	372,035	
Education:								
University of California	917,392	201,383	1,980,031	1,981,464	(1,433)	(0.1)	1,106,238	
State Universities and Colleges	195,794	164,092	1,703,187	1,732,449	(29,262)	(1.7)	1,349,688	
Other Education	17,359	13,457	123,076	130,748	(7,672)	(5.9)	113,208	
Dept. of Corrections and Rehabilitation	727,918	650,909	5,817,055	5,749,603	67,452	1.2	5,077,308	
Governmental Operations	53,183	-	439,865	488,990	(49,125)	(10.0)	-	
General Government	157,636	166,480	1,542,621	1,575,237	(32,616)	(2.1)	1,774,822	
Public Employees Retirement System	(160,800)	(144,311)	111,051	133,957	(22,906)	(17.1)	136,738	
Debt Service (d)	146,099	507,086	2,119,613	2,502,690	(383,077)	(15.3)	2,515,907	
Interest on Loans	6,354	3,177	(42,103)	(38,814)	(3,289)	-	(110,071)	
Total State Operations	2,386,599	2,042,273	17,335,469	17,685,386	(349,917)	(2.0)	15,333,793	
LOCAL ASSISTANCE (c)								
Public Schools - K-12	2,526,273	1,984,427	29,301,775	29,730,149	(428,374)	(1.4)	26,956,999	
Community Colleges	277,897	153,028	3,159,487	3,093,357	66,130	2.1	2,542,346	
Debt Service-School Building Bonds	-	-	-	-	-	-	-	
Contributions to State Teachers'								
Retirement System	-	-	870,541	870,540	1	0.0	883,975	
Other Education	182,151	243,709	1,267,049	1,381,355	(114,306)	(8.3)	1,456,935	
School Facilities Aid	-	-	-	-	-	-	-	
Dept. of Corrections and Rehabilitation	2,945	25,543	167,271	167,313	(42)	(0.0)	213,992	
Dept. of Alcohol and Drug Program	304	834	(800)	(1,655)	855	-	40,337	
Health Care Services and Public Health:								
Medical Assistance Program	1,148,416	1,254,050	12,640,265	12,292,340	347,925	2.8	11,109,931	
Other Health Care Services/Public Health	39,700	19,553	60,568	122,648	(62,080)	(50.6)	145,070	
Developmental Services - Regional Centers	125,387	219,776	2,341,200	2,428,778	(87,578)	(3.6)	2,364,715	
Department of State Hospitals	-	-	-	-	-	-	10,664	
Dept. of Social Services:								
SSI/SSP/IHSS	344,271	349,425	3,399,834	3,458,928	(59,094)	(1.7)	3,423,893	
CalWORKs	128,652	138,074	1,137,502	1,101,624	35,878	3.3	842,264	
Other Social Services	142,089	91,987	506,839	469,068	37,771	8.1	427,223	
Tax Relief	-	-	210,867	210,860	7	0.0	213,642	
Other Local Assistance	61,844	45,651	1,386,551	1,449,437	(62,886)	(4.3)	861,073	
Total Local Assistance	4,979,929	4,526,057	56,448,949	56,774,742	(325,793)	(0.6)	51,493,059	

See notes on page A1.

(Continued)

SCHEDULE OF CASH DISBURSEMENTS (Continued)

(Amounts in thousands)

	Month of February		July 1 through February 28				2013	
	2014	2013	Actual	Estimate (a)	Actual Over or (Under) Estimate			Actual
					Amount			
CAPITAL OUTLAY	925	151	133,645	147,768	(14,123)	(9.6)	103,172	
NONGOVERNMENTAL (c)								
Transfer to Special Fund for Economic Uncertainties	-	(474,757)	122,900	122,900	-	-	473,243	
Transfer to Budget Stabilization Account	-	-	-	-	-	-	-	
Transfer to Other Funds	47,245	21,800	462,199	436,948	25,251	5.8	353,344	
Transfer to Revolving Fund	34	(10)	7,078	7,045	33	0.5	5,413	
Advance:								
MediCal Provider Interim Payment	-	-	(1,000,000)	(1,000,000)	-	-	-	
State-County Property Tax Administration Program	(24,505)	(12,088)	8,541	13,745	(5,204)	(37.9)	60,671	
Social Welfare Federal Fund	(28,001)	-	(18,250)	(18,250)	-	-	(70,800)	
Local Governmental Entities	-	-	29,087	-	29,087	-	60,000	
Tax Relief and Refund Account	-	-	-	-	-	-	-	
Counties for Social Welfare	-	-	(315,672)	(315,672)	-	-	(275,732)	
Total Nongovernmental	(5,227)	(465,055)	(704,117)	(753,284)	49,167	-	606,139	
Total Disbursements	\$ 7,362,226	\$ 6,103,426	\$ 73,213,946	\$ 73,854,612	\$ (640,666)	(0.9)	\$ 67,536,163	
TEMPORARY LOANS								
Special Fund for Economic Uncertainties	\$ -	\$ (474,757)	\$ 122,900	\$ 122,900	\$ -	-	\$ 473,243	
Budget Stabilization Account	-	-	-	-	-	-	-	
Outstanding Registered Warrants Account	-	-	-	-	-	-	-	
Other Internal Sources	1,489,004	988,777	6,082,033	8,263,315	(2,181,282)	-	(3,844,832)	
Revenue Anticipation Notes	-	-	5,500,000	5,500,000	-	-	10,000,000	
Net Increase / (Decrease) Loans	1,489,004	\$ 514,020	\$ 11,704,933	\$ 13,886,215	\$ (2,181,282)	(15.7)	\$ 6,628,411	

See notes on page A1.

(Concluded)

COMPARATIVE STATEMENT OF REVENUES RECEIVED
All Governmental Cost Funds
(Amounts in thousands)

	July 1 through February 28			
	General Fund		Special Funds	
	2014	2013	2014	2013
MAJOR TAXES, LICENSES, AND INVESTMENT INCOME:				
Alcoholic Beverage Excise Taxes	\$ 236,449	\$ 221,592	\$ -	\$ -
Corporation Tax	2,838,801	2,292,843	-	-
Cigarette Tax	58,608	61,791	508,827	523,182
Estate, Inheritance, and Gift Tax	6,106	3,353	4	-
Insurance Companies Tax	1,147,101	1,105,131	248,776	13,518
Motor Vehicle Fuel Tax:				
Gasoline Tax	-	-	3,813,433	3,474,953
Diesel & Liquid Petroleum Gas	-	-	210,670	221,229
Jet Fuel Tax	-	-	2,268	1,617
Vehicle License Fees	1,666	5,679	1,437,485	1,303,588
Motor Vehicle Registration and Other Fees	-	-	2,779,929	2,603,351
Personal Income Tax	39,873,023	40,795,345	717,161	724,923
Retail Sales and Use Taxes	14,682,171	12,963,107	9,074,372	8,613,421
Pooled Money Investment Interest	14,940	14,615	83	102
Total Major Taxes, Licenses, and Investment Income	58,858,865	57,463,456	18,793,008	17,479,884
NOT OTHERWISE CLASSIFIED:				
Alcoholic Beverage License Fee	2,122	1,588	34,702	34,306
Electrical Energy Tax	-	-	404,837	384,773
Private Rail Car Tax	7,812	7,879	-	-
Penalties on Traffic Violations	-	-	40,974	43,393
Health Care Receipts	6,126	8,509	-	-
Revenues from State Lands	289,175	285,289	-	-
Abandoned Property	(14,207)	44,010	-	-
Trial Court Revenues	32,267	33,709	1,008,241	1,045,777
Horse Racing Fees	774	844	8,216	8,570
Cap and Trade	-	-	275,294	55,760
Miscellaneous	615,550	915,952	7,363,837	8,134,870
Not Otherwise Classified	939,619	1,297,780	9,136,101	9,707,449
Total Revenues, All Governmental Cost Funds	\$ 59,798,484	\$ 58,761,236	\$ 27,929,109	\$ 27,187,333

See notes on page A1.

STATEMENT OF GENERAL FUND CASH RECEIPTS AND DISBURSEMENTS
A Comparison of Actual to 2013-14 Budget Act
(Amounts in thousands)

	July 1 through February 28				
	2014				2013
	Actual	Estimate (a)	Actual Over or (Under) Estimate		Actual
			Amount		
GENERAL FUND BEGINNING CASH BALANCE	\$ -	\$ -	\$ -	-	\$ -
Add Receipts:					
Revenues	59,798,484	56,503,000	3,295,484	5.8	58,761,236
Nonrevenues	1,710,529	978,283	732,246	74.9	2,146,516
Total Receipts	61,509,013	57,481,283	4,027,730	7.0	60,907,752
Less Disbursements:					
State Operations	17,335,469	16,946,965	388,504	2.3	15,333,793
Local Assistance	56,448,949	56,924,224	(475,275)	(0.8)	51,493,059
Capital Outlay	133,645	142,208	(8,563)	(6.0)	103,172
Nongovernmental	(704,117)	(968,772)	264,655	-	606,139
Total Disbursements	73,213,946	73,044,625	169,321	0.2	67,536,163
Receipts Over / (Under) Disbursements	(11,704,933)	(15,563,342)	3,858,409	-	(6,628,411)
Net Increase / (Decrease) in Temporary Loans	11,704,933	15,563,342	(3,858,409)	(24.8)	6,628,411
GENERAL FUND ENDING CASH BALANCE	-	-	-		-
Special Fund for Economic Uncertainties	-	-	-	-	-
TOTAL CASH	\$ -	\$ -	\$ -		\$ -
BORROWABLE RESOURCES					
Available Borrowable Resources	\$ 28,392,111	\$ 27,225,100	\$ 1,167,011	(e) 4.3	\$ 33,650,891
Outstanding Loans (b)	14,139,798	17,998,206	(3,858,408)	(21.4)	16,221,702
Unused Borrowable Resources	\$ 14,252,313	\$ 9,226,894	\$ 5,025,419	54.5	\$ 17,429,189

General Note:

This report is based upon funded cash. Funded cash is cash reported to and recorded in the records of the State Controller's Office. Amounts reported as funded cash may differ from amounts in other reports to the extent there are timing differences in the recording of in-transit items.

Footnotes:

- (a) %A Statement of Estimated Cash Flow for the 2013-14 fiscal year was prepared by the Department of Finance for the 2013 Budget Act. Any projections or estimates are set forth as such and not as representation of facts.
- (b) %Outstanding loan balance of \$14.1 billion is comprised of \$8.6 billion of internal borrowing and \$5.5 billion of external borrowing. Current balance is comprised of \$2.4 billion carried forward from June 30, 2013, plus current year Net Increase/(Decrease) in Temporary Loans of \$11.7 billion.
- (c) %Negative amounts are the result of repayments received that are greater than disbursements made.
- (d) %Debt Service amounts are net of offsets such as federal subsidies and reimbursements from other sources. To the extent that these offsets do not occur when anticipated, there can be variances between actuals and estimates on a month-to-month basis.
- (e) On August 22, 2013, \$5.5 billion of Revenue Anticipation Notes (RANs) proceeds were received.

SCHEDULE OF CASH RECEIPTS

(Amounts in thousands)

	Month of February		July 1 through February 28				
			2014			2013	
	2014	2013	Actual	Estimate (a)	Actual Over or (Under) Estimate		Actual
					Amount		
REVENUES							
Alcoholic Beverage Excise Tax	\$ 27,295	\$ 41,405	\$ 236,449	\$ 226,000	\$ 10,449	4.6	\$ 221,592
Corporation Tax	124,382	144,347	2,838,801	2,646,000	192,801	7.3	2,292,843
Cigarette Tax	6,611	6,329	58,608	60,000	(1,392)	(2.3)	61,791
Estate, Inheritance, and Gift Tax	421	898	6,106	-	6,106	-	3,353
Insurance Companies Tax	16,877	18,055	1,147,101	1,134,000	13,101	1.2	1,105,131
Personal Income Tax	2,300,732	1,926,806	39,873,023	36,431,000	3,442,023	9.4	40,795,345
Retail Sales and Use Taxes	3,012,661	2,993,544	14,682,171	14,983,000	(300,829)	(2.0)	12,963,107
Vehicle License Fees	108	458	1,666	-	1,666	-	5,679
Pooled Money Investment Interest	537	732	14,940	21,000	(6,060)	(28.9)	14,615
Not Otherwise Classified	120,302	152,637	939,619	1,002,000	(62,381)	-	1,297,780
Total Revenues	5,609,926	5,285,211	59,798,484	56,503,000	3,295,484	5.8	58,761,236
NONREVENUES							
Transfers from Special Fund for Economic Uncertainties	-	-	-	-	-	-	-
Transfers from Other Funds	44,501	91,717	902,132	273,943	628,189	229.3	1,391,453
Miscellaneous	218,795	212,478	808,397	704,340	104,057	14.8	755,063
Total Nonrevenues	263,296	304,195	1,710,529	978,283	732,246	74.9	2,146,516
Total Receipts	\$ 5,873,222	\$ 5,589,406	\$ 61,509,013	\$ 57,481,283	\$ 4,027,730	7.0	\$ 60,907,752

See notes on page B1.

SCHEDULE OF CASH DISBURSEMENTS

(Amounts in thousands)

	Month of February		July 1 through February 28					2013
	2014	2013	Actual	Estimate (a)	Actual Over or (Under) Estimate		Actual	
					Amount			
STATE OPERATIONS (c)								
Legislative/Judicial/Executive	\$ 113,948	\$ 116,938	\$ 1,167,948	\$ 1,030,881	\$ 137,067	13.3	\$ 667,021	
Business, Consumer Services and Housing	943	91,196	11,572	9,792	1,780	18.2	471,532	
Transportation	-	56	464	-	464	-	2,710	
Resources	43,043	44,130	774,893	804,221	(29,328)	(3.6)	846,299	
Environmental Protection Agency	2,211	5,388	27,610	29,612	(2,002)	(6.8)	23,275	
Health and Human Services:								
Health Care Services and Public Health	19,285	65,164	213,369	207,130	6,239	3.0	204,875	
Department of State Hospitals	123,241	99,749	918,076	802,345	115,731	14.4	782,208	
Other Health and Human Services	22,993	57,379	427,141	495,095	(67,954)	(13.7)	372,035	
Education:								
University of California	917,392	201,383	1,980,031	1,267,280	712,751	56.2	1,106,238	
State Universities and Colleges	195,794	164,092	1,703,187	1,749,615	(46,428)	(2.7)	1,349,688	
Other Education	17,359	13,457	123,076	131,072	(7,996)	(6.1)	113,208	
Dept. of Corrections and Rehabilitation	727,918	650,909	5,817,055	5,717,322	99,733	1.7	5,077,308	
Governmental Operations	53,183	-	439,865	494,176	(54,311)	(11.0)	-	
General Government	157,636	166,480	1,542,621	1,469,948	72,673	4.9	1,774,822	
Public Employees Retirement System	(160,800)	(144,311)	111,051	136,438	(25,387)	(18.6)	136,738	
Debt Service (d)	146,099	507,086	2,119,613	2,659,512	(539,899)	(20.3)	2,515,907	
Interest on Loans	6,354	3,177	(42,103)	(57,474)	15,371	-	(110,071)	
Total State Operations	2,386,599	2,042,273	17,335,469	16,946,965	388,504	2.3	15,333,793	
LOCAL ASSISTANCE (c)								
Public Schools - K-12	2,526,273	1,984,427	29,301,775	29,929,936	(628,161)	(2.1)	26,956,999	
Community Colleges	277,897	153,028	3,159,487	3,136,206	23,281	0.7	2,542,346	
Debt Service-School Building Bonds	-	-	-	-	-	-	-	
Contributions to State Teachers'								
Retirement System	-	-	870,541	874,555	(4,014)	(0.5)	883,975	
Other Education	182,151	243,709	1,267,049	1,500,226	(233,177)	(15.5)	1,456,935	
School Facilities Aid	-	-	-	-	-	-	-	
Dept. of Corrections and Rehabilitation	2,945	25,543	167,271	174,194	(6,923)	(4.0)	213,992	
Dept. of Alcohol and Drug Program	304	834	(800)	-	(800)	-	40,337	
Health Care Services and Public Health:								
Medical Assistance Program	1,148,416	1,254,050	12,640,265	11,997,824	642,441	5.4	11,109,931	
Other Health Care Services/Public Health	39,700	19,553	60,568	172,323	(111,755)	(64.9)	145,070	
Developmental Services - Regional Centers	125,387	219,776	2,341,200	2,133,732	207,468	9.7	2,364,715	
Department of State Hospitals	-	-	-	-	-	-	10,664	
Dept. of Social Services:								
SSI/SSP/IHSS	344,271	349,425	3,399,834	3,556,584	(156,750)	(4.4)	3,423,893	
CalWORKs	128,652	138,074	1,137,502	1,156,425	(18,923)	(1.6)	842,264	
Other Social Services	142,089	91,987	506,839	518,247	(11,408)	(2.2)	427,223	
Tax Relief	-	-	210,867	205,967	4,900	2.4	213,642	
Other Local Assistance	61,844	45,651	1,386,551	1,568,005	(181,454)	(11.6)	861,073	
Total Local Assistance	4,979,929	4,526,057	56,448,949	56,924,224	(475,275)	(0.8)	51,493,059	

See notes on page B1.

(Continued)

SCHEDULE OF CASH DISBURSEMENTS (Continued)

(Amounts in thousands)

	Month of February		July 1 through February 28				2013	
	2014	2013	Actual	Estimate (a)	Actual Over or (Under) Estimate			Actual
					Amount			
CAPITAL OUTLAY	925	151	133,645	142,208	(8,563)	(6.0)	103,172	
NONGOVERNMENTAL (c)								
Transfer to Special Fund for Economic Uncertainties	-	(474,757)	122,900	122,900	-	-	473,243	
Transfer to Budget Stabilization Account	-	-	-	-	-	-	-	
Transfer to Other Funds	47,245	21,800	462,199	169,000	293,199	173.5	353,344	
Transfer to Revolving Fund	34	(10)	7,078	-	7,078	-	5,413	
Advance:								
MediCal Provider Interim Payment	-	-	(1,000,000)	(1,000,000)	-	-	-	
State-County Property Tax Administration Program	(24,505)	(12,088)	8,541	-	8,541	-	60,671	
Social Welfare Federal Fund	(28,001)	-	(18,250)	-	(18,250)	-	(70,800)	
Local Governmental Entities	-	-	29,087	55,000	(25,913)	(47.1)	60,000	
Tax Relief and Refund Account	-	-	-	-	-	-	-	
Counties for Social Welfare	-	-	(315,672)	(315,672)	-	-	(275,732)	
Total Nongovernmental	(5,227)	(465,055)	(704,117)	(968,772)	264,655	-	606,139	
Total Disbursements	\$ 7,362,226	\$ 6,103,426	\$ 73,213,946	\$ 73,044,625	\$ 169,321	0.2	\$ 67,536,163	
TEMPORARY LOANS								
Special Fund for Economic Uncertainties	\$ -	\$ (474,757)	\$ 122,900	\$ 122,900	\$ -	-	\$ 473,243	
Budget Stabilization Account	-	-	-	-	-	-	-	
Outstanding Registered Warrants Account	-	-	-	-	-	-	-	
Other Internal Sources	1,489,004	988,777	6,082,033	9,940,442	(3,858,409)	-	(3,844,832)	
Revenue Anticipation Notes	-	-	5,500,000	5,500,000	-	-	10,000,000	
Net Increase / (Decrease) Loans	1,489,004	\$ 514,020	\$ 11,704,933	\$ 15,563,342	\$ (3,858,409)	(24.8)	\$ 6,628,411	

See notes on page B1.

(Concluded)